S. HRG. 116–433

EXAMINATION OF THE MAIN STREET LENDING PROGRAM

HEARING

BEFORE THE

CONGRESSIONAL OVERSIGHT COMMISSION

ONE HUNDRED SIXTEENTH CONGRESS

SECOND SESSION

ON

EXAMINING THE MAIN STREET LENDING PROGRAM CREATED BY THE FEDERAL RESERVE, PURSUANT TO THE CARES ACT

AUGUST 7, 2020

Printed for the use of the Congressional Oversight Commission

Available at: https://www.govinfo.gov/

U.S. GOVERNMENT PUBLISHING OFFICE

41–488 WASHINGTON : 2021

CONGRESSIONAL OVERSIGHT COMMISSION

FRENCH HILL, Representative	DONNA E. SHALALA, Representative
BHARAT RAMAMURTI, Commissioner	PATRICK J. TOOMEY, Senator

AMBER VENZON, *Chief Clerk*

EXAMINATION OF THE MAIN STREET LENDING PROGRAM ESTABLISHED BY THE FEDERAL RESERVE PURSUANT TO THE CARES ACT

FRIDAY, AUGUST 7, 2020

U.S. CONGRESS,
CONGRESSIONAL OVERSIGHT COMMISSION,
Washington, DC.

The Commission met by videoconference and in person, pursuant to notice, at 10:02 a.m., in Room G50, Dirksen Senate Office Building, the Hon. French Hill, Acting Chairman, presiding.

Present: Representative Hill, Mr. Ramamurti, Representative Shalala, and Senator Toomey.

OPENING STATEMENT OF MR. HILL

Mr. HILL. The hearing will come to order.

This is a hearing, a hybrid hearing, meaning that some of our Commissioners are appearing in person and witnesses will testify remotely. Before I begin, let me offer a few videoconferencing reminders.

Once before you start speaking, there will be a slight delay before you are displayed on the screen. To minimize background noise, please click the mute button until your turn to speak or to ask a question. If there is a technology issue, we will move to the next speaker until it is resolved.

You should all have one box on your screens labeled "Clock" to show you how much time is remaining. All members and witnesses need to be especially mindful of the 5-minute clock. At 30 seconds remaining, I will gently tap the gavel to remind members that their time has almost expired.

To simplify the speaking order process, the Commission has decided to order ourselves alphabetically.

With that, welcome to this virtual hearing convened by the Congressional Oversight Commission. Pursuant to Section 4020 of Title IV subtitle of the CARES Act, the Commission must conduct oversight of the $500 billion authorized for the Exchange Stabilization Fund. As a part of our oversight work, the Commission has decided to hold this hearing today which will examine the Main Street Lending Facilities.

The Federal Reserve established the Main Street Lending Program to support lending to small and medium-sized businesses and nonprofit organizations that were in sound financial condition before the onset of the COVID–19 pandemic. The program operates through five facilities which we will learn more about this morning.

The program is being administered by the Federal Reserve Bank of Boston. Today's hearing will have two panels. President Eric Rosengren, President and Chief Executive Officer of the Federal Reserve Bank of Boston will testify during the first panel, and the second panel will include industry participants.

In the absence of a Chair, the Commissioners have agreed to each have 1 minute of opening remarks. I will now recognize myself for an opening statement.

Our Commission is pleased to convene this hearing of the Main Street Lending Program. Thank you to our witnesses for lending your expertise today. I believe this is an extremely timely and important discussion.

I also commend my fellow Commissioners. Together we have worked in a bipartisan, bicameral way to release three reports and organize this inaugural hearing.

I would also like to thank our personal staffs for their diligence in this area, particularly in the absence of a Chair, and on behalf of all Commissioners, I welcome our new Chief Clerk, Amber Venzon, and thank you to the U.S. Senator for these facilities today. Findings from today's hearing will be reflected in our next report.

The Main Street Lending Program term sheet was released on April 9th and finally became operational on July 6th. Leading to its implementation, the program generated significant interest and engagement. However, in the months since the program has been available, $95 million of the $600 billion allocated has been loaned to eligible businesses. I hope we find answers today that will help explain why it took 3 months to stand up the program and what, if anything, needs to be done to alter the program to expand the universe of eligible borrowers.

I yield back, and I now recognize Commissioner Ramamurti for 1 minute.

OPENING STATEMENT OF MR. RAMAMURTI

Mr. RAMAMURTI. Thank you, Mr. Chairman, and thank you to each of the witnesses appearing today.

Four months ago, Congress gave the Treasury Department half a trillion dollars to stabilize the economy. The Treasury quickly pledged $75 billion of those dollars to the Federal Reserve's Main Street Lending Program for small and mid-sized companies. After taking 3 months to set up the program, the Fed has now been operating it for about a month. In that time, it has supported only 18 loans for a total of $104 million. That is 0.017 percent of the $600 billion lending capacity that the Fed touted for the program in April.

While all this money has been sitting on the sidelines, tens of thousands of businesses have permanently closed, and millions of Americans have lost their jobs. By any measure the Main Street Program has been a failure. My goal today is to figure out why the program has failed and how to fix it quickly before more Americans lose their jobs and more good businesses have to shut their doors.

Thank you, Mr. Chairman.

Mr. HILL. Thank you, Commissioner.

I now recognize Congresswoman Shalala for 1 minute.

OPENING STATEMENT OF MS. SHALALA

Ms. SHALALA. Thank you. Good morning. I would like to thank our witnesses for being here today. I represent Florida's 27th Congressional District, which includes most of Miami-Dade County.

COVID–19 is out of control in my district. We have a raging community spread. As a result, we have a financial disaster with 50 percent of businesses laying off workers and others going bankrupt.

In South Florida, our economy is heavily reliant on tourism. Actually, we are reliant on crowds. Unlike big businesses that can rely on capital markets for funding, small and mid-sized businesses are more susceptible to being permanently shut down.

Recognizing this, we approved funding in the CARES Act in March to support up to $600 billion in lending to these businesses. However, while some Florida businesses have benefitted from the Main Street loans, what has been accomplished to date is simply not enough.

We all agree that these businesses need help to survive the crisis, and I am here today to understand why the money has not been deployed and what the impact has been on workers.

I yield back.

Mr. HILL. Thank you, Congresswoman.

I now recognize Senator Toomey for 1 minute.

OPENING STATEMENT OF SENATOR TOOMEY

Senator TOOMEY. Thank you very much, Mr. Chairman, and I also want to thank all the witnesses for participating in this hearing today.

Look, I think the big questions that I am looking forward to learning about is certainly why relatively few borrowers have participated in this program, why it appears not to have a tremendous amount of demand. I want to understand whether through this program banks are likely to originate loans that they would not otherwise engage in anyway. And at some point, we need to have a discussion about the fact that we are in a different place than we were when we first designed these programs back in March.

We intended, at least I did as one of the negotiators of this legislation, to provide liquidity so that business could survive what we hoped would be a very brief, although we knew would be a severe downturn. Now we have the prospect of possibly excess capacity in a number of industries that could persist for some time. That is a new and different challenge.

So I look forward to exploring all of these and, again, want to thank the witnesses for joining us.

Mr. HILL. Thank you, Senator Toomey.

All Commissioners' statements will be added to the hearing record. We are fortunate today to have five witnesses appearing and appreciate their time.

President Rosengren is the President and CEO of the Federal Reserve Bank of Boston, one of the 12 regional Federal Reserve banks. Dr. Rosengren is a participant in the Federal Open Market Committee, the monetary policymaking arm of the United States.

As CEO, he leads the Boston Fed's work, which includes economic research and analysis, banking supervision and financial stability efforts, community economic development activities, and a wide range of payments, technology, and finance initiative.

Ms. Lauren Anderson serves as the senior vice president and associate general counsel of the Bank Policy Institute. In this role, she oversees the BPI's advocacy across a range of domestic and international issues. She brings with her over a decade of experience in financial regulation and resolution oversight, most recently serving as the senior adviser at the Bank of England and, before joining the Bank of England, served as Special Adviser to the Deputy of Policy at our FDIC.

Mr. Tom Bohn serves as the chief executive officer of the Association for Corporate Growth. ACG serves 90,000 investors, executives, lenders, and advisers to the growing middle-market set of companies. Prior to joining ACG in December 2019, Mr. Bohn served as CEO of the North American Veterinary Community where he oversaw unprecedented growth.

Mr. Vince Foster serves as the executive chairman of the Main Street Capital Corporation, a position he has held since November of 2018. Mr. Foster previously served as Main Street's CEO from 2007 until November of 2018 and served as Main Street's president from 2012 to 2015. He also has been a member of the management team's investment committee since its formation. Main Street Capital offers capital solutions for lower middle-market companies.

And our final witness, Ms. Gwen Mills, secretary-treasurer of UNITE HERE. Ms. Mills has been working with UNITE HERE for 20 years. She served as the political director from 2015 to 2017 and was elected secretary-treasurer in 2017. UNITE HERE has 300,000 members, largely serving the travel and tourism industry.

We will now proceed to President Rosengren's testimony. He will testify, and we will move into two rounds of 5-minute questioning. Immediately following the questioning, I will recognize the second panel of witnesses for their testimony, and then we will move into that questioning. Each of the witnesses' full written testimony will be made a part of the official hearing record.

President Rosengren, welcome, and you are now recognized for 5 minutes.

STATEMENT OF ERIC S. ROSENGREN, PH.D., PRESIDENT AND CHIEF EXECUTIVE OFFICER, FEDERAL RESERVE BANK OF BOSTON

Mr. ROSENGREN. Representative Hill, Commissioner Ramamurti, Representative Shalala, and Senator Toomey, thank you for the opportunity to speak about the Main Street Lending Program, which the Boston Fed administers for the Federal Reserve System. My written testimony contains charts and details I hope will be useful to you, but I will be brief in this overview.

In addition to tragic loss of life, the pandemic poses an unprecedented shock to our economy. Many entities impacted by the pandemic rely on bank for loans. The Main Street Program is designed to facilitate lending to small and medium-sized businesses and nonprofits that have suffered disruptions. It provides credit support for entities that have temporary cash flow problems due to the pandemic and that, given the uncertain outlook, may have difficulty obtaining credit. It can provide a bridge as loans have no interest or principal payments in the first year and no principal payments until year 3.

Unlike facilities that purchase standardized credit instruments, this program purchases interests in loans that are, by nature, bespoke agreements often with complex, borrower-specific terms and conditions. Since our portal opened for registration on the 15th of June, 509 institutions have registered, and their assets represent over $14 trillion, about 58 percent of banking assets in the United States.

Main Street relies on lenders to underwrite loans and keep skin in the game by banks retaining 5 percent of the loan. Borrowers need to meet the lender's underwriting standards and the program's terms and conditions and be able to make certifications and commitments, including those required by the CARES Act.

The program includes three loan facilities for for-profit businesses and two for nonprofits that have been announced but are not yet live. Nonprofits and their lenders can, nonetheless, use the published terms and documents to begin discussing program loans. I will describe early results.

As of Tuesday, over $530 million in loans are active in the portal, 54 loans. Eighteen loans with a combined value of $109 million have our commitment for purchase or have settled. We opened for purchases on July 6th, and the numbers are consistent with the gradual pace of the initial activity, more recently expanding.

The 54 loans submitted represent 29 distinct lenders. The largest number of loans are by institutions in the $10 to $50 billion range, but relatively small community banks have participated. To date, there has been limited activity by banks with over $50 billion in assets.

But the program's modest initial numbers seem to be giving way to more uptake as participants and banks become more familiar with the program. Quickly scaling up a program that purchases participations in loans from diverse borrowers in a decentralized market that lacks standardization is inherently difficult and a significant achievement.

The eventual size of the program will be determined by the path of the pandemic and the economy. Should conditions worsen, which we hope does not happen, I would expect interest to expand more rapidly. Credit interruptions prolong recessions and harm individuals. In administering the program, we will do all in our power and purview to support the firms, nonprofits, and workers that make up our Nation's economy.

Thank you for the opportunity to provide this overview. I would be happy to address any questions.

[The prepared statement of Mr. Rosengren follows:]

Eric S. Rosengren, President and CEO, Federal Reserve Bank of Boston

Prepared Testimony for the Congressional Oversight Commission

August 7, 2020

Members of the Commission – Representative Hill, Mr. Ramamurti, Representative Shalala, and Senator Toomey – thank you for the opportunity to speak with you about the operationalization of the Federal Reserve's Main Street Lending Program, a facility authorized by the Board of Governors of the Federal Reserve System ("Board of Governors") under section 13(3) of the Federal Reserve Act, with approval of the Secretary of the Treasury. As you know, the Department of the Treasury ("Treasury") has committed to make an equity investment of $75 billion in the Program – and the funds available for investment by the Treasury were appropriated to the Exchange Stabilization Fund under section 4027 of the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act").

The Federal Reserve Bank of Boston, which I lead, administers the operations of the Main Street Lending Program ("Main Street" or "Program") for the Federal Reserve System. As such, I am very pleased to be here today to provide information that I hope will be useful to you in your important oversight work.

Background to the Program

In addition to the tragic loss of life, all of us know that the COVID-19 pandemic poses a shock to the U.S. economy that is unprecedented in our lifetimes. With real GDP in the second quarter falling by more than 30 percent, it is clear that businesses, nonprofits, and individuals across the country are being challenged by the fallout from the virus. We have seen a disproportionate impact on entities whose operating models require significant social interaction, stemming from consumers' concern with their own health and safety as well as more formal restrictions on movement and commerce. For example, hotels, airlines, retail stores, entertainment venues, restaurants, and tourism-related enterprises have all suffered significant disruptions to their businesses and cash flow, with more difficulties possible if the public health concerns persist. Nonprofit entities like medical service providers and educational institutions also are challenged.

Both fiscal and monetary policymakers have acted swiftly to address the economic impacts of the pandemic and cushion the blow. The Federal Reserve, for example, has taken a number of aggressive policy actions since late winter, aimed at blunting the economic effects of the crisis. Seeing unusual volatility and troubled financial markets, the Federal Open Market Committee reduced short-term interest rates to near zero and purchased significant amounts of securities, and the Board of Governors established a variety of emergency facilities under section 13(3) of the Federal Reserve Act in order to restore market functioning and facilitate lending.

These actions helped to restore financial stability and significantly reduced spreads on short- and long-term corporate and municipal securities – spreads which had increased due to uncertainty, and challenged the flows of credit that underpin our economy. And the facilities helped to unlock a great deal of private credit, as well.

Many of the emergency lending facilities are similar to facilities rolled out during the 2008-2009 financial crisis. However, many of the businesses most impacted by the pandemic are smaller firms that rely on banks for loans, rather than accessing public credit markets (i.e., issuing bonds). The Main Street Lending Program is designed to facilitate lending to small and medium-sized businesses that have suffered disruptions from the pandemic, and were in sound condition prior to the pandemic. The program, like all emergency lending facilities, was authorized by the Board and Treasury, and in this case is being implemented and administered by the Federal Reserve Bank of Boston.

The terms of the Main Street Program were enhanced and expanded by the Board and Treasury prior to the Program's opening, and more recently a term sheet has been released that makes the Program available to non-profit organizations as well as for-profit businesses. I would note that in addition to providing loans for borrowers in current need of funds, the Program offers a credit backstop for firms that do not currently need financing, but may if the pandemic continues to erode the financial condition of these firms over late summer and fall.

Importantly, the Main Street Lending Program differs from other programs for businesses made possible by the CARES Act, reflecting the parameters of what the Federal Reserve is authorized by Congress to do. Unlike the Paycheck Protection Program, where many loans could turn into *grants* funded by the CARES Act, the Main Street program involves loans that must be repaid. The Program has no loan guarantee like the Small Business Administration provided for the Paycheck Protection Program, and requires both the borrower and lender to be eligible to participate in the Program.

We engaged in a great deal of consultation with potential borrowers and lenders as we set up the Program. In addition to soliciting public comment, staff at the Board of Governors, Treasury, and the Federal Reserve Bank of Boston conducted outreach to potential borrowers and lenders of all sizes – ranging from community banks to the largest lenders in the country – in an effort to gather information to inform policy judgments and operational decisions related to the Program. In addition to the variety of outreach calls, we have hosted a series of 14 (so far) webinars that have been tailored to borrowers and lenders, and in which presenters review the terms, conditions, and operational details of the Program. All of the sessions have been well attended with many having more than 1,500 participants.

To ensure the Program is widely known, in conducting these webinars and otherwise sharing information we have made an intentional effort to reach nonprofits, minority and women-owned businesses, minority depository institutions, and tribal businesses. In addition, robust Frequently Asked Questions documents provide detail on many aspects of the for-profit and non-profit program facilities, and are updated with some frequency.

Parameters of the Program

The Main Street Lending Program was designed to provide credit support for business or nonprofit borrowers that have temporary cash-flow problems due to the pandemic – and given the uncertain outlook might otherwise have difficulty in obtaining credit from a lender that would have to hold 100 percent of the loan. Main Street can provide a loan to bridge the borrower over this current challenge. Main Street loans have no interest or principal payments in the first year, and indeed no principal payments until year three, making the cash-flow aspects of the loan attractive to borrowers experiencing a pandemic-related, temporary disruption of their business model.

The Program includes three lending components for for-profit businesses. They have similar interest rates, maturities, and terms, but have somewhat different collateral arrangements, loan-size limitations, and underwriting. For mid-sized businesses with existing term or revolving lines of credit, the Main Street *Expanded* Loan Facility (MSELF) allows businesses to upsize their current loans, with additional lending of $10 million to $300 million. For smaller businesses, the Main Street *Priority* Loan Facility (MSPLF) allows businesses to borrow from

$250,000 to $50 million. Under each of these facilities the Main Street loans must be senior or *pari passu* (of equivalent status) with the borrower's other loans and debt instruments (excluding mortgage debt).

For smaller business loans without collateral, there is the Main Street *New* Loan Facility (MSNLF) that provides loans from $250,000 to $35 million dollars, which cannot be contractually subordinated to other debt. Because these loans do not have security or collateral requirements, they are only available for firms whose debt including the Main Street loan does not exceed four times the borrower's EBITDA – a more restrictive underwriting criterion than the other two loan types, which set maximum loan size based on six times the borrower's EBITDA.

The two *nonprofit* lending components of Main Street are announced but not yet live. They will have broadly similar terms as the for-profit Main Street facilities, for example in maturity and interest rate. The Nonprofit Organization *Expanded* Loan Facility (NOELF) and the Nonprofit Organization *New* Loan Facility (NONLF) have similar priority and size requirements to their for-profit counterparts. They differ in that the underwriting is tailored to the special characteristics of nonprofits.

Lending, and Lenders

We have taken great care to operationalize the Main Street program to ensure it functions smoothly and securely. Of course, setting up a program to serve many different borrowers and lenders is inherently complex, but I believe the Commission in its oversight role can feel confident that this challenge is being met in strong fashion, in the public interest.

Unlike the corporate credit and muni facilities, which purchase largely standardized credit instruments, Main Street purchases interests in loans that are, by nature, bespoke agreements between borrowers and lenders. Loan agreements and loan terms can be quite different across banks, and even within a bank the agreements are the result of negotiation between borrower and lender that often result in complex, borrower-specific terms and conditions. For example, banks differ on whether they require personal guarantees or collateral in excess of Program requirements; and those policies may vary based on the financial condition or business model of the borrower.

Constructing a Program that handles this complexity is something we have been intensely engaged with these last few months at the Federal Reserve Bank of Boston. We are pleased to have the opportunity to do this important work, in the spirit of public service that runs through our work and our staff.

Shifting to how the program works, to become an eligible lender for the Program the financial institution must first register via our Main Street lender portal. As part of the enrollment process, the institution must verify that it meets our eligibility requirements, and make attestations regarding CARES Act provisions which require the signature of the principal executive officer and principal financial officer. Furthermore, the institution must set up and verify arrangements to transfer funds effectively and safely, to ensure security and resilience.

Since our portal opened for lender registration on June 15, 509 financial institutions have registered with the Program, and their assets represent $14.25 trillion, which is approximately 58 percent of total banking assets in the United States. The attached **Figure 1** shows the size distribution of registered MSLP lenders. It includes the largest universal banks and regional banks, and a sizable number of banks in the $1-10 billion asset range as well as in the under $1 billion asset category. Participation is of course strictly voluntary for financial institutions.

During the extensive outreach that we did prior to launching Main Street, we heard concerns from some businesses that their current lender would not be participating in the Program or that they might find it difficult to locate a participating financial institution that would work with new customers. In aiming to address these concerns, we ask lenders during the registration process if they plan to accept loan applications from new customers. We contact each lender that says they would consider loan applications from new customers, and ask whether they will join a public list of such lenders. **Figure 2** shows the interactive map we created that allows borrowers to identify which lenders in their state are registered with Main Street, are prepared to consider new customers, and are willing to be listed as such. The interactive map is available on the program website, www.bostonfed.org/mslp, and we update the list daily as new lenders register. Currently it contains 153 lenders. Figure 2 shows, for an example, the financial institutions on the map for my home state of Massachusetts.

It is important to note that Main Street relies on lenders to underwrite the loans, and indeed the lenders have "skin in the game" by retaining 5 percent of the loan participation. Borrowers need to meet the underwriting standards of the financial institution, and the terms and conditions of the Main Street Lending Program, whether they have an existing relationship with the lender or are a new customer.

Borrowers also must meet the eligibility criteria set out in the Program term sheet, and must be able to make the certifications and commitments required by the Program, including those required under the CARES Act. Also, while the loan interest rate of 300 basis points over LIBOR is likely attractive to somewhat higher-risk borrowers, those businesses that have strong balance sheets and have *not* been significantly impacted by the pandemic may very well find their lender can give them more attractive terms than the Main Street Program. Because the loans are not forgivable by the Federal Reserve and lenders retain a 5 percent interest in the loan, borrowers must have the ability to pay back the loan. For borrowers with severe problems, additional debt may not be helpful, and neither the lender nor the borrower will find taking additional debt attractive. But for many others, the program can serve as a vital bridge to address cash flow interruption ushered in by the pandemic.

Early Results

Figure 3 shows the flow of potential loan participation purchases through the Program's portal as of the end of the day on Tuesday (August 4). As you see on the summary bottom line, currently over $530 million in loans are active in the portal, representing 54 loans. Of that total, 18 loans with a combined value of $109 million have commitments for purchase or have been settled. In addition, over $421 million in loans are in various stages of review in the portal. As a reminder, the program opened for loan purchases on July 6. The numbers I share with you today are consistent with what I would characterize as a gradual pace of initial activity, which is more recently expanding.

The 54 loans submitted in the portal currently represent 29 distinct lenders. Almost all the loans currently in the portal have been initiated by financial institutions with under $50 billion in assets. Additionally, there are 36 lenders with *draft* entries in progress in the system. I mention these draft entries because they reinforce that additional lenders are active in the portal and getting familiar with Program operations.

Figure 4 breaks out the total of potential loans in the portal by the particular branch or facility of the Program. The largest number of loans – 29 – are in the New Loan Facility. The Priority Loan Facility currently has 24 loans valued at $328 million in the portal. And currently there is only one loan utilizing the Expanded Loan Facility in the portal. The Expanded loan facility will generally encompass larger loans and require current participating banks to alter existing loan agreements to upsize existing credit facilities.

Figure 5 provides the size distribution of potential loans currently in the portal. While the largest number of loans are in the size cohort between $1 million and $2.5 million dollars, there are loans under $1 million and greater than $30 million. The industries represented include construction and design firms, dental offices, retailers, and entertainment-related firms like movie theaters. Thus, the loans we have seen to date have reflected what one might broadly expect of small and mid-sized firms whose businesses have been disrupted by the current efforts at social distancing.

Figure 6 shows the potential loan distribution by the asset size of the lender registered in the Program. The largest number of loans are by financial institutions in the $10-50 billion size range. However, there has been participation by relatively small community banks as well. To date, there has been only limited activity by banks with more than $50 billion in assets.

As I alluded to a moment ago, the Program's relatively modest initial numbers seem to be giving way to more uptake as participants become familiar with the program's parameters. I believe the gradual uptake is a function of participants adjusting to a few unavoidable factors. First and foremost, loans are bespoke, and the Program needs to accommodate lending across a wide range of industries, jurisdictions, and business profiles, which makes for operational challenges. Also, the Program's complexity reflects the underlying loan agreements, the terms and conditions in the Program, and requirements related to the CARES Act. As a result, it can take some time for borrowers and lenders to gather the required documents for submission to the Program. Loan documents not in compliance with terms and conditions have slowed some of the intake. We are working to help participants understand and avoid common errors that can slow the process down.

Summary Observations

Designing and operationalizing a program of this breadth and nuance, delivered through highly secure technology, is a significant achievement in a few months' time. Everyone involved is focused on helping to provide important credit support to businesses and nonprofits at this critical and challenging time.

As we speak today, in early August, I can say that we have worked through many challenges. Among the emergency lending facilities established by the Federal Reserve since late winter – and indeed in comparison to the emergency programs of the 2008 financial crisis – the Main Street Lending Program is operationally complex. Quickly scaling up a program that purchases participations in bespoke loans – from a very diverse group of borrowers in a decentralized market that lacks standardization – is inherently difficult. There are also tradeoffs between limiting credit risk, targeting support, reaching scale, and achieving operational efficiency. Considerations such as these have made the Main Street Lending Program one of the most challenging emergency lending programs the Federal Reserve has ever put in place. The Commission can be assured that the Federal Reserve and Treasury have sought to design a program that is well managed with respect to risks, efficiency, and resilience, while being responsive to the needs of borrowers experiencing difficult times.

The eventual size of the Program will be determined by the path of the pandemic and the economy, generally. Should the pandemic and the economy worsen, or financial institutions experience larger than expected loan losses and depletion of capital – all things we hope do not happen – then I would expect interest in using this Program to expand more rapidly.

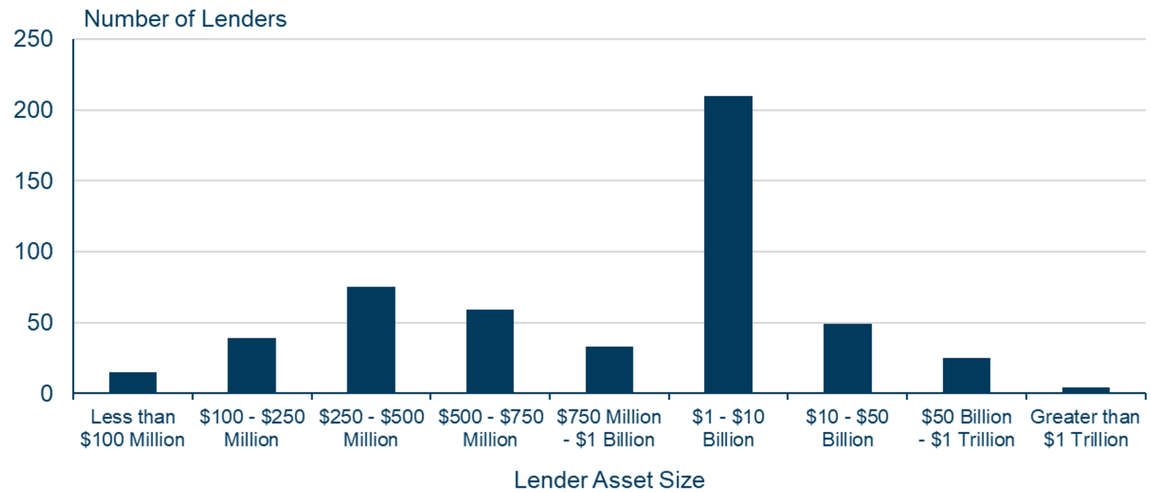
In conclusion, the pandemic's shock to our economy is unprecedented, and the pain for businesses, organizations, and workers has been unparalleled in our lifetimes. It is important that the Federal Reserve stands ready at this time of distress, in the public interest and in pursuit of our Congressional mandates, to support lending to for-profit businesses and nonprofit organizations of many sizes at reasonable rates. From many decades of research and policymaking, I can attest that credit interruptions prolong recessions and ultimately harm individuals on Main Streets across America. I pledge to you that in administering the Program, the Boston Fed and the Federal Reserve as a whole will do all that is in our power and purview to effectively support the firms, nonprofits, and individuals that make up our nation's economy.

Thank you for the opportunity to provide this high-level overview of the Program. I would now be happy to address any questions.

Figures included in the Prepared Testimony of
Eric S. Rosengren
President and CEO
Federal Reserve Bank of Boston
for the Congressional Oversight Commission

August 7, 2020

Figure 1: Asset Size Distribution of MSLP Registered Lenders

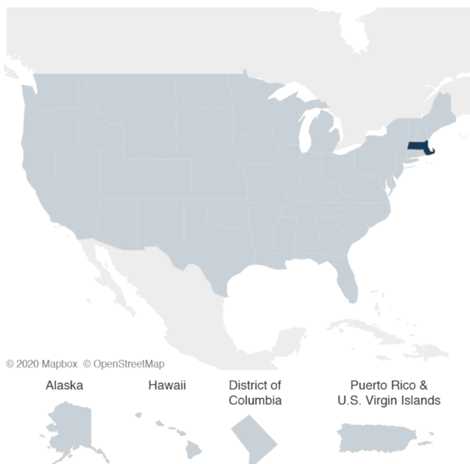


Note: Registered lenders totaled 509 as of August 4, 2020.

Source: Federal Reserve Bank of Boston

Figure 2: Interactive Map of MSLP Registered Lenders by State

Select your State



Select a Lender

BANK OF AMERICA	Businesses ✓ | Nonprofits ✓
CITIZENS BANK	Businesses ✓ | Nonprofits ✓
ENVISION BANK	Businesses ✓ | Nonprofits ✓
FALL RIVER FIVE CENTS SAVINGS BANK	Businesses ✓ | Nonprofits ✓
GFA FEDERAL CREDIT UNION	Businesses ✓ | Nonprofits ✓
HARBOR BANKSHARES ASSET MANAGEMENT, LLC	Businesses ✓ | Nonprofits ✓
JPMORGAN CHASE & CO	Businesses ✓ | Nonprofits ✓
KEYBANK	Businesses ✓ | Nonprofits ✓
NEW VALLEY BANK & TRUST	Businesses ✓ | Nonprofits ✓
PEOPLE'S UNITED BANK	Businesses ✓ | Nonprofits ✓
SANTANDER BANK	Businesses ✓ | Nonprofits ✓
STERLING NATIONAL BANK	Businesses ✓ | Nonprofits ✓
STONEHAMBANK	Businesses ✓ | Nonprofits ✓
WEBSTER BANK	Businesses ✓ | Nonprofits ✓
WEBSTER FIVE CENTS SAVINGS BANK	Businesses ✓ | Nonprofits ✓
WORKERS CREDIT UNTION	Businesses ✓ | Nonprofits ✓

Listing of Lenders Accepting New Customers

Borrowers can view a state-by-state listing of lenders participating in the Main Street Lending Program who are currently accepting applications from new customers by viewing the interactive map.

This list reflects a subset of the lenders participating in the Main Street Lending Program — specifically, lenders registered for the program who are accepting applications from new customers, in addition to existing ones; and also elect to be listed.

Source: Federal Reserve Bank of Boston, Interactive Map

Figure 3: MSLP Loans to Borrowers by Status

Processing Status as of August 4, 2020	Number of Loans	Participation Amount	Loan Amount
Loans Committed or Settled	18	$104,006,000	$109,480,000
Loans Under Review	36	$400,327,014	$421,396,857
Total	54	$504,333,014	$530,876,857

Note: Additionally, there were 36 lenders with 53 draft entries in progress in the system, reinforcing that lenders are active in the portal and getting familiar with program operations.

Source: Federal Reserve Bank of Boston

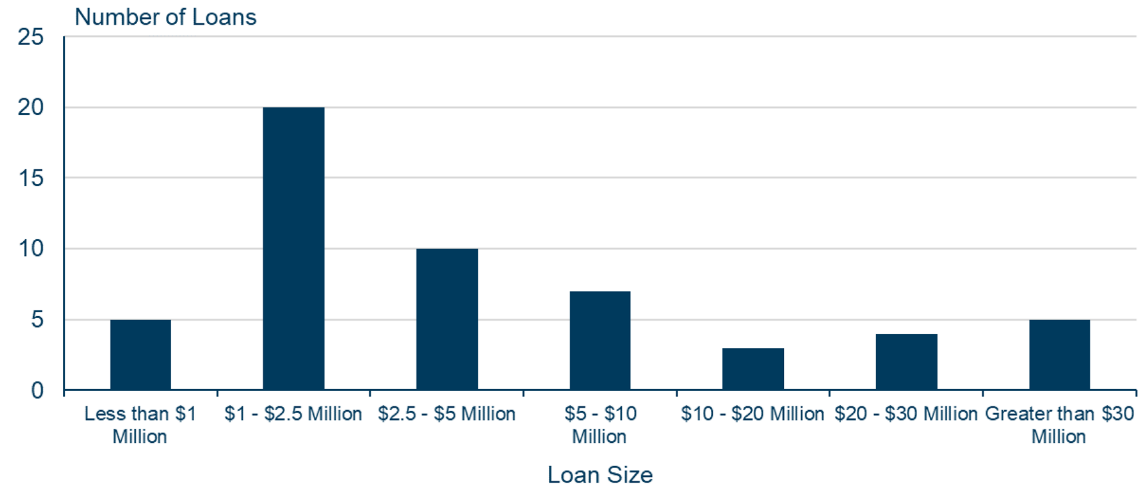
Figure 4: MSLP Loans to Borrowers by Facility

Facility	Number of Loans	Participation Amount	Loan Amount
New Loan Facility	29	$126,445,901	$133,100,948
Expanded Loan Facility	1	$66,001,250	$69,475,000
Priority Loan Facility	24	$311,885,864	$328,300,909
Total	54	$504,333,014	$530,876,857

Note: Additionally, there were 36 lenders with 53 draft entries in progress in the system, reinforcing that lenders are active in the portal and getting familiar with program operations.

Source: Federal Reserve Bank of Boston

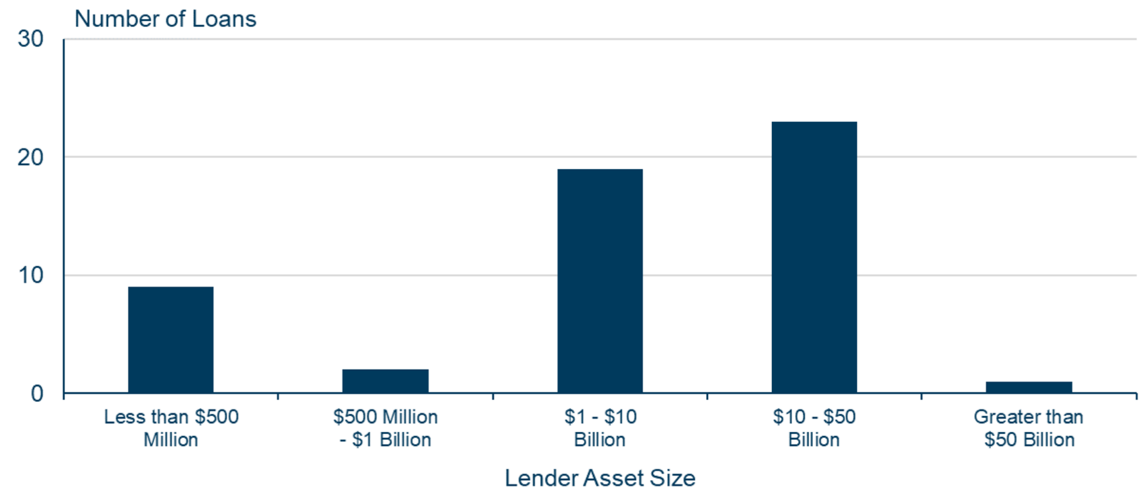
Figure 5: Distribution of MSLP Loans to Borrowers by Loan Size



Note: Does not include the additional 53 draft entries which include loans as large as $47.5 million.

Source: Federal Reserve Bank of Boston

Figure 6: Distribution of MSLP Loans to Borrowers by Asset Size of MSLP Registered Lender



Note: Does not include the additional 53 draft entries which include loans as large as $47.5 million.

Source: Federal Reserve Bank of Boston

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August 31, 2020

Mr. Bharat Ramamurti, Commissioner
Congressional Oversight Commission
Washington, D.C. 20510

Dear Commissioner Ramamurti:

Enclosed are my responses to the questions you submitted following the August 7, 2020,[1] hearing before the Congressional Oversight Commission.

Please let me know if I may be of further assistance.

Sincerely,

Eric Rosengren

Enclosure

[1] Questions related to this hearing were received on August 14, 2020.

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Follow-Up Questions Submitted to President Eric Rosengren, Federal Reserve Bank of Boston (Witness Name) from Commissioner Ramamurti

Question 1: Many smaller cities, towns, school districts, and other public entities like hospitals function much like non-profits—both in terms of the essential role they play in our communities and with respect to how they obtain credit, with bank lending to local governmental entities constituting a large share of all outstanding municipal credit.[2] The Municipal Lending Facility (MLF) is ill-suited to serving these smaller governmental entities, who cannot participate directly in the MLF. Moreover, they may have trouble participating indirectly in the MLF through larger borrowers like state governments. Has the Federal Reserve considered whether there are unmet credit needs of such smaller governmental borrowers that could be met by expanding the MSLF to encompass them? Please explain whether the Federal Reserve believes such an expansion warranted.

In general, the Federal Reserve believes that the Municipal Liquidity Facility (MLF) is the best tool to address the liquidity challenges in the municipal bond market through which these entities normally obtain credit, rather than the Main Street Lending Program (Main Street or Program), which is a loan participation program. The purpose of the MLF is to enhance the liquidity of the municipal securities market by increasing the availability of funding to eligible issuers through purchases of their short-term notes. By addressing the cash management needs of eligible issuers, the MLF was also intended to encourage private investors to reengage in the municipal securities market, including across longer maturities. The MLF also encourages eligible issuers to borrow on behalf of and lend to smaller local governments and other entities that are not otherwise eligible for direct participation in the MLF. As a result of the deployment of the MLF and other Federal Reserve monetary tools, the municipal market has substantially recovered from its unprecedented sell-off in March and the vast majority of municipal issuers currently have access to capital at historically low costs of funds.[3] We will continue to closely monitor conditions in the markets for municipal securities and will evaluate whether additional measures are needed to support the flow of credit and liquidity to state and local governments.

The Main Street facilities for nonprofit organizations also have a role to play in providing credit to certain public entities, including public hospitals and public colleges and universities, that operate in a manner similar to other types of nonprofit organizations recognized as tax-exempt pursuant to 501(c)(3) of the Internal Revenue Code. The Federal Reserve has published the requirements that such public entities must meet to qualify as eligible borrowers for purposes of the Main Street facilities for nonprofit organizations. The eligibility criteria for the nonprofit lending facilities were designed in light of underwriting standards often applied by lenders in making loans to nonprofit borrowers, including nonprofit hospitals, colleges, and universities that have a similar financial profile to their public counterparts. The Federal Reserve is currently working to create the infrastructure necessary to fully operationalize the Main Street facilities for nonprofit organizations.

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[2] Ivanov, Ivan and Tom Zimmerman, "The Privatization of Municipal Debt," Brookings Institution Hutchins Center Working Paper #45 (Sept. 2018), *available at* https://www.brookings.edu/wp-content/uploads/2018/08/WP45.pdf.
[3] https://libertystreeteconomics.newyorkfed.org/2020/06/municipal-debt-markets-and-the-covid-19-pandemic.html.

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Question 2: In a recent study examining the Payment Protection Program (PPP) administered by the Small Business Administration, the Federal Reserve Bank of New York found "significant coverage gaps" in the PPP's ability to reach Black-owned businesses, despite the pandemic's outsized impact on communities of color.[4] Will the Federal Reserve conduct a similar study of whether and how the CARES Act programs that it administers have impacted racial and ethnic minorities?

The Federal Reserve has taken a number of actions to facilitate broad coverage by Main Street. Recognizing that the circumstances, structure, and needs of small and medium sized for-profit and nonprofit organizations vary considerably, the Federal Reserve sought feedback from a wide range of potential borrowers, lenders and the general public on the proposed terms of the facilities to help make the Program as efficient and effective as possible. Based on this feedback, the Federal Reserve has modified the terms of the Program to provide greater access to credit for small and medium-sized for-profit and nonprofit organizations that were in sound financial condition prior to the pandemic.

To provide potential lenders with information about Main Street and to address their questions in real time, to date the Federal Reserve has held (and posted recordings of) 14 webinars and conducted a number of other events (including three in collaboration with the Small Business Administration) explaining aspects of the Program and engaging in question and answer sessions. On June 24, the Federal Reserve hosted a webinar on Main Street targeted toward minority- and women-owned businesses, and on August 4, the Federal Reserve hosted a webinar targeted toward tribal businesses. The Federal Reserve is conducting additional outreach to raise awareness of the program among women- and minority-owned businesses and in low- and middle-income communities, including sharing program information and updates with more than 70 associations and networks working with minority-owned and women-owned businesses.

To encourage their involvement, the Federal Reserve has also conducted outreach to minority depository institutions (MDIs) and community development financial institutions (CDFIs) to provide opportunities to learn about the Program. On July 1, as part of the Federal Reserve's Partnership for Progress program, staff of the Federal Reserve Board and FRBB, together with the National Bankers Association, held a briefing on Main Street for MDIs. On August 4, Federal Reserve Board and FRBB staff attended a National Business Inclusion Consortium event to present the details of the Main Street Program. On August 12, staff participated in an event sponsored by the Department of Commerce's Minority Business Development Agency and provided a Main Street Program overview.

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[4] Claire Kramer Mills, "Double Jeopardy: COVID-19's Concentrated Health and Wealth Effects in Black Communities," Federal Reserve Bank of New York (Aug. 2020), *available at* https://www.newyorkfed.org/medialibrary/media/smallbusiness/DoubleJeopardy_COVID19andBlackOwnedBusinesses.

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These efforts will contribute to broad coverage. The Federal Reserve will continue to assess the efficacy of the Program, including its effects on low-income or minority communities.

Question 3: Will the Federal Reserve collect and report any data on whether minority-owned businesses are participating in the MSLF program?

The Federal Reserve will collect and disclose information regarding Main Street during the operation of the facilities, including information regarding names of lenders and borrowers, amounts borrowed and interest rates charged, and overall costs, revenues, and other fees. The Federal Reserve does not plan to collect information on minority status of borrowing entities. We will continue to conduct outreach sessions to underserved communities to promote Program awareness. Further, we will continue to monitor broader credit conditions across different communities and geographies and weigh adjustments needed to reach eligible borrowers.

Question 4: President Rosengren testified that Federal Reserve's outreach plan for the MSLF included an intentional effort to reach minority and women-owned businesses, minority depository institutions, and tribal businesses. What further steps is the Federal Reserve taking to ensure that the MSLF program is made available on an inclusive basis? For example, in light of reports of lending discrimination by banks participating in the PPP,[5] what steps will the Federal Reserve take to ensure that banks participating in the MSLF offer MSLF-backed loans on a non-discriminatory basis?

As indicated in response to Question 2, the Program is designed to have wide coverage, and the Federal Reserve has conducted outreach targeted toward minority, women-owned, and tribal businesses, as well as MDIs and depository CDFIs.

All eligible lenders under Main Street are federally regulated financial institutions, subject to ongoing federal supervision. Such lenders are instructed to employ their existing underwriting processes in relation to Main Street loans, and to use loan documentation that is substantially similar, including with respect to required covenants, to the loan documentation that the eligible lender uses in its ordinary course lending to similarly situated borrowers, adjusted only as appropriate to reflect the requirements of the Program. By structuring the Program in this way, the Federal Reserve expects that Main Street loans would be subject to the same regulatory infrastructure and supervisory scrutiny (including by the Federal Reserve, where applicable) as other loans made by the eligible lenders. As such, any discriminatory behavior by lenders will be addressed as appropriate under the law.

Question 5: In response to questions about whether certain MSLF program terms and requirements were changed in response to requests from the oil and gas industry, President Rosengren testified that "[i]n the discussions [he] ha[s] been involved in, we do not discuss

[5] *Anneliese Lederer, et al., "Lending Discrimination within the Paycheck Protection Program," National Community Reinvestment Coalition (July 2020), available at* https://www.ncrc.org/lending-discrimination-within-the-paycheck-protection-program/.

specific industries." However, the Energy Secretary has stated publicly that he and Treasury Secretary Mnuchin worked with the Federal Reserve to ensure that the energy industry could participate in the Federal Reserve's lending facilities.[6] Is President Rosengren aware of any discussions, deliberations, meetings, or communications in which specific industries or companies were discussed—irrespective of whether he was personally involved in those discussions? If so, please identify what officials or agencies may have been involved.

The Main Street facilities are intended to improve financial or credit conditions broadly, not to allocate credit to narrowly defined sectors, industries, or classes of borrowers. I am not aware of any conversations regarding how the terms and conditions of the Main Street facilities would apply to oil and gas companies beyond conversations discussing how Main Street would apply to broad sectors of the economy.

From time-to-time, the needs of specific industries or types of borrowers are raised in internal discussions and deliberations in relation to Main Street. In designing the Program, the Federal Reserve received more than 2,200 comments from businesses of all sizes, across industries, and representing many sectors of the economy. Federal Reserve staff has considered issues pertaining to particular companies or industries — including manufacturers, commercial real estate companies, and retailers — when such concerns are raised by members of Congress or other public commenters. However, any decisions that the Federal Reserve has made in designing the Program were intended to meet the needs of a wide range of businesses across the economy, not in response to any particular industry's concerns or to ensure any particular industry's participation.

Question 5: The Federal Reserve publicly disclosed public comments that it received, which reportedly were the basis for changes to the MSLF made on April 30, 2020.[7] However, some of the changes made on April 30, 2020 are not reflected in any of those publicly disclosed comments, such as the deletion of the required attestation that the loan was needed "due to the exigent circumstances presented by the … COVID-19 pandemic." As the public record currently stands, the only evidence of anyone requesting that change and certain other changes is that they were requested only by the oil and gas industry,[8] and that requests by

[6] *E.g.*, Timothy Gardner, "Trump administration working to ease drilling industry cash crunch," Reuters (Apr. 17, 2020), *available at* https://www.reuters.com/article/us-health-coronavirus-usa-oil-credit/trump-administration-working-to-ease-drilling-industry-cash-crunch-idUSKBN21Z1JY; Saleha Mohsin & Ari Natter, "Energy Chief Says Fed Asked to Expand Lending for Oil Firms," Bloomberg.com (May 12, 2020), *available at* https://www.bloomberg.com/news/articles/2020-05-12/energy-chief-says-fed-was-asked-to-expand-lending-for-oil-firms.

[7] *See* Press Release, "Federal Reserve Board announces it is expanding the scope and eligibility for the Main Street Lending Program," Federal Reserve (Apr. 30, 2020), *available at* https://www.federalreserve.gov/newsevents/pressreleases/monetary20200430a.htm (citing public comments as basis for loan term sheet adjustments).

[8] *E.g.*, Letter to Secretary Mnuchin and Chairman Powell from Senator Ted Cruz (Apr. 24, 2020), *available at* https://www.cruz.senate.gov/files/documents/Letters/4.24.2020%20Oil%20Gas%20Fed%20Lending%20Facility%20Letter.pdf (stating that "condition…that a borrower must attest they require financing because of circumstances attributed to COVID-19…may prove to be too restrictive" "in the context of energy").

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that industry were sometimes made outside the ordinary public comment process available to everyone else.[9] Will the Federal Reserve publicly disclose all documents, communications, and records of communications that relate to the energy industry's participation in the MSLF?

When issuing the April 30, 2020 term sheets, the Federal Reserve and Treasury made a number of changes to the attestations that would have been required under the initial April 8, 2020 term sheets in light of the public comment period and further internal discussion and analysis. In particular, a number of changes were driven by comments raising questions about the precise meaning of certain proposed attestations, how borrowers and lenders could determine and evidence their compliance with such requirements, and how such attestations would be enforced. In the course of this careful review and rationalization, it was determined that there was not sufficient reason to retain the initially proposed borrower attestation that a loan was needed "due to the exigent circumstances presented by the … COVID-19 pandemic." The following considerations informed this decision:

- Due to the widespread effects of the pandemic, the Federal Reserve and Treasury anticipated that nearly all borrowers that would desire to access Main Street would have been affected adversely by the pandemic. Further, the Federal Reserve and Treasury determined that it would be difficult for many businesses to evidence the pandemic's effect on their business outside of pointing to decreased demand, which may not conclusively demonstrate a connection to the pandemic.[10]

- Under the Board's Regulation A, each borrower must certify that it is unable to secure adequate credit accommodations from other banking institutions. It was determined that this required certification would serve much of the same purpose as the removed attestation, because each address whether the Program is being used as a back-stop.

- Under section 13(3) of the Federal Reserve Act and the Board's Regulation A, each borrower must certify that it is not "insolvent." As clarified in the Main Street Borrower Certifications and Covenants, a borrower is insolvent if it has been "generally failing to pay undisputed debts as they become due" during the 90 days preceding the date of borrowing to the extent it is behind on its debts for reasons other than disruptions to its business resulting from the pandemic. For those behind on their debts due to the pandemic, the borrower is considered insolvent if it was generally failing to pay its undisputed debts in the 90 days

[9] *E.g.*, Timothy Gardner, "Trump administration working to ease drilling industry cash crunch," Reuters (Apr. 17, 2020), *available at* https://www.reuters.com/article/us-health-coronavirus-usa-oil-credit/trump-administration-working-to-ease-drilling-industry-cash-crunch-idUSKBN21Z1JY (reporting Energy Secretary's statement that he met with U.S. energy industry representatives to discuss the size of loans they would need in order to participate in the MSLF).

[10] Similar concerns were raised by other commenters, including on p. 63 of the document, *available at* https://www.federalreserve.gov/monetarypolicy/files/mslp-public-comments-202007015.pdf; and p. 41 of the document *available at* https://www.federalreserve.gov/monetarypolicy/files/mslp-public-comments-202007016.pdf. In addition, during outreach to a trade association representing companies of all sizes and across all sectors, concerns were raised that this particular attestation could trigger material adverse change clauses in borrower's existing debt covenants.

preceding the later of March 1, 2020, or the date on which changes in its business activity related to the COVID-19 pandemic commenced. It was determined that this required attestation would serve much of the same purpose as the removed attestation by focusing on the financial condition of the borrower outside of the effects of the pandemic.

- The Program requires that any outstanding loans that the eligible borrower had with the eligible lender as of December 31, 2019, must have had an internal risk rating equivalent to a "pass" in the Federal Financial Institutions Examination Council's supervisory rating system on that date. A borrower meeting this criteria, but desiring a Main Street loan, is likely to have been adversely affected by the pandemic. It was determined that this requirement would serve much of the same purpose as the removed attestation by focusing on the financial condition of the borrower prior to the pandemic.

The Federal Reserve has disclosed the comments it received during the comment period, including those submitted by or on behalf of the oil and gas industry.

Question 6: Title 12 U.S.C. § 343(3) and 12 C.F.R. § 201.4 require the Federal Reserve's emergency lending programs to be "broad-based." In the Federal Reserve's view, as a legal matter, do these provisions permit changes to a program designed to benefit a particular industry or particular companies, so long as the program as a whole has broad eligibility? Please explain the Federal Reserve's view of what the broad-based requirement does and does not encompass.

Consistent with section 13(3) of the Federal Reserve Act, all of the Federal Reserve's facilities have broad, neutrally defined eligibility requirements and pricing mechanisms and are designed to minimize credit allocation while also minimizing risk to the taxpayer.[11] As the Federal Reserve and Treasury stated in March 2009, "actions taken by the Federal Reserve should aim to improve financial or credit conditions broadly, not to allocate credit to narrowly-defined sectors or classes of borrowers."[12]

The Federal Reserve Board formally interpreted the statutory "broad-based" requirement at 12 CFR 201.4(d)(4), which clarifies that "a program or facility has broad-based eligibility only if [it] is designed to provide liquidity to an identifiable market or sector of the financial system," and that a program or facility is not considered broad-based if it is designed to aid one or more failing companies, or if fewer than five persons or entities would be eligible to participate.[13]

[11] 12 U.S.C. § 343(3).
[12] Joint Press Release, The Role of the Federal Reserve in Preserving Financial and Monetary Stability Joint Statement by the Department of the Treasury and the Federal Reserve (Mar. 23, 2009), *available at* https://www.federalreserve.gov/newsevents/pressreleases/monetary20090323b.htm.
[13] 12 CFR 201.4(d)(4)(ii)-(iii).

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Question 7: For the Secondary Market Corporate Credit Facility (SMCCF), the Federal Reserve has stated that it will leverage the Treasury equity at a ratio as low as 3 to 1,[14] while the MSLF appears to have a larger equity cushion. Is the Federal Reserve more willing to absorb risks with respect to the SMCCF than with respect to the MSLF? If so, why?

The Secondary Market Corporate Credit Facility (SMCCF) uses credit ratings to identify which debt instruments it may purchase and how much Treasury equity will be allocated to protect against losses from those instruments. The historical default rates of companies rated below investment grade are higher than those of companies rated above investment grade, but the SMCCF adjusts for heightened credit risk by allocating more Treasury equity to support purchases of companies rated below investment grade. In particular, the SMCCF leverages the Treasury equity at 10 to 1 when acquiring corporate bonds of issuers that are investment grade but only at 7 to 1 when acquiring corporate bonds of issuers that were previously rated investment grade but are now rated one rating grade below investment grade. When the SMCCF purchases exchange-traded fund (ETF) shares, it leverages the Treasury equity at between 10 to 1 and 3 to 1, depending on the risk profile of the ETF.

For Main Street, which lends primarily to companies that were in sound financial condition prior to the onset of the COVID-19 pandemic, and to companies for which a credit rating is usually not readily available, the Federal Reserve has leveraged the $75 billion equity investment at a maximum of 8 to 1. We feel that this ratio is appropriate given the creditworthiness of the borrowers for whom Main Street was designed.

Question 8: Has the Federal Reserve analyzed whether more companies would be served by the MSLF if the loan term were extended an additional year or more? Please explain whether the Federal Reserve believes such an extension warranted.

The five-year maturity for Main Street loans facilitates the provision of credit over the medium-term to bridge near-term cash flow disruptions that result from the COVID-19 pandemic. A longer maturity may contribute to the ability of some borrowers to repay a loan. A longer maturity may also increase risk to lenders or the taxpayer. The five-year maturity balances these competing considerations.

We will continue to monitor lending conditions broadly and consider adjustments to Main Street terms and conditions, as appropriate, working with the Department of the Treasury which has made an equity investment in a Special Purpose Vehicle (Main Street SPV) in connection with the Program. The facility was established by the Federal Reserve under the authority of Section 13(3) of the Federal Reserve Act, with approval of the Treasury Secretary.

[14] Terms Sheet, Secondary Market Corporate Credit Facility, Federal Reserve (July 28, 2020), *available at* https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200728a1.pdf.

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Question 9: Has the Federal Reserve analyzed whether Community Development Financing Institutions (CDFI) are able to originate MSLF loans? Please explain whether the Federal Reserve believes any changes to the MSLF would be needed to facilitate participation by CDFIs that serve low-income and minority communities, and whether it believes such changes warranted?

CDFIs that are depository institutions are eligible lenders under Main Street. At this time, nonbank CDFIs are not considered eligible lenders for purposes of the Program. Some aspects of the Program may limit participation by eligible CDFIs, which often originate loans smaller than the minimum Main Street loan or that emphasize underwriting criteria that differ from those used by Main Street. The Federal Reserve will continue to analyze these issues. As emphasized in my testimony and responses to questions at the hearing, adjustments to the Program, including a lower minimum loan size, would provide benefits but also entail operational costs, and there may be more efficient approaches to supporting CDFIs and the communities they serve than adjustments to Main Street.

Question 10: Has the Federal Reserve analyzed whether lowering the minimum loan size further would facilitate participation by more businesses with unmet needs? Please explain whether the Federal Reserve believes such changes warranted. To the extent the Federal Reserve believes a lower loan size would present administrability issues given the capacity of the Boston branch to oversee this complex program, has it considered creating another facility administered by a branch other than Boston?

In order to manage the operational elements of the Program, we have maintained a minimum loan size of $250,000. Allowing for smaller loans may increase the number of businesses that wish to participate in the Program. However, managing intake and credit administration during the life of the loan for many thousands of small loans would require significant additional operational capacity on the part of lenders. In addition, the fixed costs for both borrowers and lenders of legal and accounting fees and administration costs of originating and administering loans would be very high as a percentage of the loan amount for smaller loans. The additional volume and the costs of originating smaller loans could therefore reduce lenders' willingness to participate in the Program.

We will continue to monitor credit conditions for small businesses to determine if additional adjustments to the Program are needed.[15] And the Federal Reserve will continue to assess the optimal arrangements for administering programs, in the public interest.

Question 11: Has the Federal Reserve analyzed whether decoupling lender fees from loan size could better incentivize lenders to identify and onboard smaller borrowers? Please explain whether the Federal Reserve believes higher fees for smaller-size loans could better incentivize lenders to originate loans.

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[15] To date, there has been limited uptake for loans near the Program's $250,000 minimum loan size.

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The fee structure on each of the Main Street facility loan products is a fixed percentage of the principal amount of the loan at the time of origination or upsizing. The fee is designed to cover costs of underwriting the loan and incentivize eligible lenders to participate in the Program. Linking fees to loan size is also a standard industry practice. While higher fees for origination of smaller loans may provide some incentives to lenders, higher fees would also place additional burden on smaller borrowers. Changes of this type would need to be considered in terms of their overall effect on Program operations and efficacy; in this regard, it may be useful to assess the potential benefits and costs of such adjustments relative to adjustments to other government programs to support lending to small businesses that have the experience and expertise to execute such programs quickly and effectively.

As with other aspects of Main Street, we will continue to monitor the efficacy of the fee structure and will make adjustments as necessary.

Question 12: Were the MSLF affiliation rules to be relaxed, what would prevent private-equity companies from transferring wealth out of the borrowing business to the private-equity sponsor, and what kinds of restrictions would prevent such wealth transfers?

To determine eligibility for Main Street, a business must aggregate the employees and 2019 revenues of the business itself with those of the business's affiliated entities in accordance with the affiliation test set forth in 13 CFR 121.301(f) (1/1/2019 ed.). This affiliation test applies to private equity-owned businesses in the same manner as any other business subject to outside ownership or control. As a result, some businesses owned by private equity companies are not eligible to participate in Main Street, or are otherwise constrained in the amount they can borrow due to maximum loan size restrictions on borrowing by an affiliated group.

Should such restrictions be amended, and a greater share of businesses affiliated with private-equity companies become eligible borrowers, restrictions on capital distributions and the repayment of debt owed to private-sector lenders would limit the ability of such businesses to transfer funds to the private-equity sponsor.

Question 13: Were the MSLF to be expanded to include an asset-based lending facility, how would the Federal Reserve ensure that assets are appropriately appraised, particularly in light of the significant uncertainty surrounding how COVID-19 will impact commercial propriety values? Would the Federal Reserve be equipped to oversee and enforce appraisals, so that taxpayers are not on the hook if private parties' appraisals turn out to be overvalued?

Main Street currently focuses on cash flow-based lending, for which adjusted earnings before interest, taxes, depreciation, and amortization (EBITDA) is a key underwriting metric used by lenders in evaluating the credit risk of small and medium-sized businesses. The Federal Reserve recognizes that, for some borrowers, collateral values or other factors are more indicative of the ability to obtain credit than cash flows. Staff continue to monitor lending conditions broadly. If credit conditions for collateral-based borrowing deteriorate or other factors indicate strains on borrowers or lenders in these markets, the Federal Reserve would carefully evaluate whether its authorities could support the availability of credit.

If conditions warrant adjusting Main Street in a manner that relied on collateral values as a complement or replacement to the ratio of debt to adjusted EBITDA in determining maximum loan size, the Program would need to have features to protect taxpayers against losses. Among these features would be the amount of collateral required and how such collateral would be valued. Analysis of these issues would be important before establishing such a loan option.

Question 14: Were the MSLF to be expanded to include an asset-based lending facility, would the Federal Reserve be prepared to foreclose on assets if the borrower lacks the cash-flow to make loan payments? How would the Federal Reserve administer foreclosures?

If conditions warranted adjusting Main Street in a manner that relied on collateral values as a complement or replacement to the ratio of debt to adjusted EBITDA in determining maximum loan size, the Program would need to have features to protect taxpayers against losses. Among these features would be the process for recovering value from collateral in the event of default. Analysis of these issues would be important before establishing such a loan option.[16]

[16] In connection with the existing Main Street facilities, the Federal Reserve has stated that, consistent with Section 13(3) of the Federal Reserve Act and the Federal Reserve's obligations under the CARES Act, the Main Street SPV will make commercially reasonable decisions to protect taxpayers from losses on Main Street loans and will not be influenced by non-economic factors when exercising its rights, including with respect to a borrower that is the subject of a workout or restructuring.

Mr. HILL. Well, thank you, Mr. President, for your testimony, and I will recognize myself for 5 minutes of questions.

First, let me say that I was pleased to see the CFO confidence survey from Duke University recently showing that business believes that they are doing better than maybe they thought they would at this stage of business reopening and that market access is improving. They are concerned mostly about obviously the demand for their products.

Also, I was encouraged yesterday that 1.8 million jobs were created and that the unemployment rate fell to 10 percent. We still have a long way to go, and we are going to be talking about that today as we still have over 10 million people eager to go back to work.

And then in my home State of Arkansas, we had a very positive week in the sense that tax revenues, particularly sales tax revenues, were actually over trend and set a record. Our income taxes were 4 percent over forecast, and our sales taxes were 16 percent over forecast and 15 percent over 2019. So, clearly, the economy is reopening, and as Senator Toomey says, we have to keep that in mind as we think through these Federal Reserve facilities and what their best structure should be to accelerate that and get more people back to work in this country.

I am concerned, Mr. Rosengren, about the affiliation rules. When I looked at the Main Street term sheets, I am concerned about two things. One, it took 3 months to get the program up and running, and I would like you to address that first. And, secondly, it appears to me in this middle market that these affiliation rules that the Federal Reserve has adopted in the Main Street Program really are a significant barrier to more entrepreneurial middle-size companies that do not have access to PPP and do not have access to the public markets to have access. And I wondered why the Fed, in your view, adopted the SBA 7(a) type limitations on affiliation rules. Could you handle those two for me, please?

Mr. ROSENGREN. Certainly. First, why don't I address the question that you raised in your opening statement and have in this question about why it took so long for this facility to get set up.

This facility is very different than some of the other traditional kinds of facilities that central banks operate during a time of crisis. So most of our facilities operate through markets. Market securities, you can purchase them very easily through the market. They clear usually in a couple days, depending on the security. So it is relatively easy to quickly purchase a large number of securities and hold those securities over time.

This facility is facility we did not have during the financial crisis and really tries to get to a different segment of the population, which is those businesses that are bigger than the PPP program was designed for and smaller than what the corporate facilities are designed for.

Bank loans are inherently difficult because they are an agreement between a bank and a borrower. They take a long time for banks to negotiate with the borrower, and this facility has a variety of complex elements including the requirements of the CARES Act and the 13(3) requirements.

So in order to design this program, we first had an initial term sheet. There were very substantial revisions to that term sheet. Again, we came out with another term sheet, which was then again revised. And each of those times where we revised the term sheet, we were expanding the ability of more businesses to access the facility.

So the types of changes that were made included lowering the loan size, changing the repayment terms, and lowering the Fed participation amount.

The final term sheet for the for-profit businesses started on June 8th. On June 15th, we had the lender registration, and on July 6th, we had loan participation intake. I would highlight as part of this process that it is a highly automated process. We have to do programming, so we needed the legal documents to be in order. We needed the final term sheet to be completed, and we needed to be able to do the programming and then check and make sure that the programming worked as expected and met all the security needs of this program.

So that does take some time. It did take time to start up. And I think that gives you some idea of the complexity of the program and why it took so longer.

Mr. HILL. Yes. Thank you for that. I think the key thing is if we want to change the program, you do not anticipate it taking another 3 months to produce a different kind of Main Street term sheet if that were necessary.

Mr. ROSENGREN. It would depend on what the nature of the term sheet changes were. If the term sheet does not affect the underlying legal documents, it is much easier to implement. So there are changes that have been made as we have had changes in the term sheet. That is true for the nonprofit term sheet as well. Depending on the nature of what the changes were would determine how long it took us to actually get set up.

Mr. HILL. Thank you, sir, very much. I yield back and turn to Commissioner Ramamurti for 5 minutes of questioning.

Mr. RAMAMURTI. Thank you, Mr. Chairman.

President Rosengren, you admit that the Main Street Program is off to a slow start, but your testimony is that interest in the program will likely pick up if "the pandemic and the economy worsen."

But if you look at the data, Main Street companies are already getting crushed. The latest middle-market indicator and economic outlook survey of executives of mid-sized companies shows that, in the second quarter, these companies experienced the largest decline in employment in the survey's history. They also had the biggest drop-off in revenue in the survey's history.

Other surveys like the U.S. Chamber of Commerce's Middle Market Business Index show the same thing: massive layoffs and furloughs and widespread revenue declines.

So my question is: How much worse do things have to get before companies are interested in the Main Street Lending Program?

Mr. ROSENGREN. Well, I think we actually have seen significant pickup recently in the portal. Just as an example, there were $109 million in loans committed or settled as of last Tuesday, and 2 days later we now have 29 loans and $189 million. So there is a pickup in volume. It is particularly in the community and mid-sized banks.

Similarly, we had $530 million in loans in the portal 2 days ago. As of last night, that is $635 million.

And so I think this is early stages of this program, and the reason is because banks and borrowers have to negotiate the terms. They had to know what the term sheet was. They had to understand the characteristics of the program and how the portal worked. And so it takes some time for the banks and the borrowers to get familiar with the program and to start pledging those loans to the facility.

So in the first couple of weeks, the banks have not completed that process, and the borrowers have not completed the process, and there was not much volume. And we are slowly seeing an increase in volume over time that I would expect to continue.

So one of the challenges with trying to deal with bank loans as opposed to securities is it does not happen quickly. If you talk to large firms about a renegotiation of a line of credit, it can frequently take many, many months before they get the negotiation completed.

So one of the advantages of a bank loan is that you are able to tailor it to the needs of the borrower and the bank. There are conditions that a different bank may put on that same kind of loan, and there are a lot of differences across both banks and borrowers and what these loan agreements look like. So this is——

Mr. RAMAMURTI. Thank you, President Rosengren. In the interest of time I will move on, and I will just note that even $530 million, which you said is in the pipeline right now, that is still a tiny fraction of the total lending capacity that was created for this program.

Look, as I said in my opening remarks, I think this program has been a failure, and the basic reason for that is that the Fed could only offer loans. The data show that companies, even distressed companies, are not looking for loans. Just this week, the Fed released a survey of senior loan officers finding that, in the second quarter of 2020, demand for loans from companies of all sizes went down. Similarly, the most recent National Federation of Independent Business Survey of small businesses found that only 3 percent of business owners reported that all their borrowing needs were not satisfied. And in the testimony they submitted today, the Bank Policy Institute, which represents some of the biggest banks in the country, said they have seen "a lack of demand for Main Street Program loans from their clients."

So, President Rosengren, if the Main Street Program can only offer loans and it is clear that most small and mid-sized firms are not looking for loans right now, even though they are already struggling badly, then how is this program going to stop widespread business closures and job losses?

Mr. ROSENGREN. So this program is tailored to organizations that will be helped by loans. So if you are a business that has had no problem from the pandemic and have a pristine balance sheet, you are probably going to get better financing than the Main Street Program provides. If you are a business that is deeply troubled and is in danger of closing imminently, this program is not going to solve the problem because debt does not solve that kind of problem, equity does.

This program is designed for a business that had a disruption in short-term credit, that was in good shape prior to the crisis, and who, after the pandemic subsides, would be able to be a viable business as well. There are businesses that fit those characteristics. We are seeing some of those businesses actually coming to the facility. I am expecting over time that we will see more pickup.

Again, we are seeing some significant activity by some of the community banks and mid-sized banks, particularly those located in States like Florida, Texas, and places that have been badly impacted by the pandemic recently.

Mr. RAMAMURTI. Okay. Thank you, President Rosengren. Look, I recognize that you and the Fed staff have done a lot of work on this, but I think the issue is that the Fed is trying to solve a problem that does not exist and it is incapable of solving the problem that does exist. By law, the Fed can only support loans, and more loans are not the answer here for most companies. And this is a giant hole in our economic response to the crisis. Congress helped small businesses through the PPP. Congress helped large companies that are big enough to issue bonds by empowering the Fed to purchase corporate bonds and reduce the cost of borrowing. But the only thing that the Government has offered all these companies in between is the Main Street Program, and it is just not working. And these mid-sized companies employ 45 million people and represent a third of private-sector GDP.

So, look, I do not think continuing to tweak this program is going to work. I think Congress needs to act to provide direct support to mid-sized firms and for that money to come with real strings attached so the money benefits working people.

Thank you, Mr. Chairman.

Mr. HILL. The gentleman yields back. Thank you.

Congresswoman Shalala is recognized for 5 minutes.

Ms. SHALALA. Thank you. Let me follow up a little on that. Particular sectors like the hospitality industry have been very hard hit by the virus, in my district in particular. And as has been noted, only $109 million of the $600 billion has been injected into the economy.

I want to know whether there is actually a design flaw, not the issue that Bharat raised about whether we should have this program at all, but whether it is designed in a way which is another way of getting at that. In particular, some have suggested the terms of the program, such as the leverage ratio requirements and the loans' priority and security requirements, are better designed to protect the Government from losses than the provide liquidity to a broad range of small and mid-sized businesses.

Could you respond to that?

Mr. ROSENGREN. Yes. So this program is designed as a cash flow program. So it is designed for a business that expects to be able to pay off the debt and pay off the debt with the cash flow from its normal business operations. So that first for many businesses. It does not fit for all businesses.

For the smallest type of businesses, I agree that the PPP program is a much better program for them. It is more of a grant program than it is a debt program, and debt may not help them in that situation.

In terms of the underwriting standards, the debt-to-EBITDA standard follows industry practice. So depending on which of the facility parts, you either have a debt-to-EBITDA of 4 or a debt-to-EBITDA of 6. Many fellows expect to have a debt-to-EBITDA below that, and so I think that this program actually closely mirrors the kind of coverage that NAB banks themselves are expecting when they are looking for a loan to be bankable. So it is a combination of an underwriting standard—there are not many underwriting standards in this program. It is basically a debt-to-EBITDA and the fact that the bank is willing to underwrite the loan themselves and take a 5-percent stake.

Ms. SHALALA. The Federal Reserve recently reported that banks were actually tightening their credit standards due to the uncertain economic outlook that has resulted from the pandemic. The Fed allows banks to use these tighter credit standards in determining whether or not to make a loan under the Main Street Lending Program. If the goal is to get money out to needy borrowers, doesn't the policy of letting the banks use their tighter credit standards undermine that goal?

Mr. ROSENGREN. So the challenge is that this is a lending program, and so loans have to be paid back. And we are asking banks to voluntarily participate in the program, and we are asking banks to be sure that when they underwrite the loan, it is a loan that is to a business that has had their credit disrupted, but that over time you expect it to be a thriving business. So that does not qualify all businesses. It qualifies a particular kind of business that is appropriate for this program.

So business has been disrupted, and it is likely to be suffering. That is not attractive for this program, and from the perspective of the bank, they might not be willing to do that loan otherwise. Let me just give a simple example: a movie theater. So if you are a movie theater located in Miami and you have been closed in the spring, you opened up temporarily, and now you may have to be closed again because of the restrictions either imposed at the State level or because people do not want to be in a movie theater at a time of a pandemic.

The bank may be quite uncertain about when that loan would actually be paying because they do not know how long the pandemic will occur; they do not know when there will be a vaccine or a treatment and might not be willing to take that loan at this kind of rate given that uncertainty.

So because they are providing 95 percent of the loan to the Federal Reserve, they might be willing to provide support to that movie theater because the bulk of the risk is being taken by the Federal Reserve. So this is a lending program. It is focused on, in part, getting most of these loans paid. That is a requirement of the 13(3) procedures.

Ms. SHALALA. Ms. Anderson, who is here on behalf of the Bank Policy Institute, suggested in her written testimony that if the Fed wants banks to lend to borrowers who do not meet the bank's current underwriting standards, which have tightened in response to the economic uncertainty caused by the pandemic, the Fed must modify the design of the program to provide downside credit risk protection. In making this observation, she cites the negative treatment of these loans by regulators as disincentivizing banks to loosen their underwriting standards.

Has the Fed considered this issue?

Mr. ROSENGREN. Yeah, we have spent quite a bit of time thinking about the supervisory issues related to these loans. So the pandemic, like other natural disasters, if there was a hurricane that hit Miami, we then use guidance to make clear that we want to have a little more leeway given to those loans because of the nature of the crisis that occurred. The same thing has been done for this pandemic. So we have asked our bank examiners to work with bank management in the instances in which we are making a decision such as a Main Street loan where the borrower has been disrupted. The other regulators have agreed to this and are following the same general guidelines. So I think that in the end the loan has to have the same classification standards that a standard loan does, but the regulators now are looking at loans a little bit differently and asking the banks to work with their borrowers.

Mr. HILL. Thank you.

Mr. ROSENGREN. And that is what they are doing for the pandemic. That is what we do during other natural crises.

Mr. HILL. Thank you, Doctor. The gentlewoman's time has expired.

Senator Toomey.

Senator TOOMEY. Thanks, Mr. Chairman. Dr. Rosengren, thank you for testifying today.

Let me just start by pointing out, you know, Government money can never be a replacement for an economy, and we have spent many hundreds of billions of dollars covering 8 weeks of payroll for very small companies. This program was never designed to pick up the tab for the payroll of the American workforce.

What it was designed to do, as I recall, was to provide emergency liquidity in the hopes that it would keep viable companies alive so that workers would have a place to go back to. Part of the reason that we made unemployment benefits so much more generous than they have ever been in the history of the country is because we knew that it was inevitable that in a very, very severe, hopefully brief recession, there would unavoidably be people laid off who had no work to do because in some cases their companies were closed, forbidden from working.

What I would like to understand—and this has come up, and maybe this is just another way to think about this, but to what extent do you think that the loans that have been made so far through this program are loans that would not have been made in the absence of the program? In other words, is this designed in such a way that the only loans that are going to take place are loans that would have happened anyway, especially given the underwriting requirements on the banks and their required participation?

Mr. ROSENGREN. I mean, these loans have a different characteristic than the traditional bank loan, so it is not traditional that you have no payment of principal or interest the first year and no payment of principal the second year. That really is designed for disrupted cash flow with the ability of the borrower over time to actually be able to make payments.

When we have talked to some of the banks that have been making the loans, they have told us that these are loans that more than likely they would not have made in the absence of this program. The reason is because there is a great deal of uncertainty right now.

Congresswoman Shalala highlighted the uncertainty and the survey of terms of lending that she cited. Uncertainty is very, very high right now, and that is a situation where banks become more reluctant to lend because they do not know what the condition of the borrowers will be. So I do think that this plays an important role in reducing the risk, and if the pandemic gets worse in the fall, as at least some epidemiologists are saying, this program will probably be more extensively used.

I completely agree with your observation that a 13(3) facility does not solve the pandemic problem. It is primarily a public health problem. But we can certainly mitigate the costs of that public health problem by trying to help those businesses that have been disrupted, but were very good businesses prior to the pandemic and will be very good businesses after the pandemic.

Senator TOOMEY. And just a technical question about the fee structure because it is a little confusing the way it appears in the term sheets. When a bank makes a loan and 95 percent of it is taken by the Fed, the fee structure that the bank keeps, certainly they have the net interest income that they can earn on the 5 percent that they keep. The fee structure, which if it is 100 basis points, which I think is contemplated in the term sheet, does the bank keep 100 basis points on the 5 percent that it keeps and the balance goes to—how does that fee structure work out?

Mr. ROSENGREN. It is on the total loan. This is an incentive for the banks to participate in the program.

Senator TOOMEY. So the banks start off with 20 percent of their credit exposure in fee income. Is that correct?

Mr. ROSENGREN. That is correct, but there are costs to doing the underwriting of the loan.

Senator TOOMEY. Of course there are. But if you do a large—that is extremely unusual, right? One of the—so that would appear on the surface to be an inducement and encouragement and incentive to take more risk. But the banks are institutionally not oriented towards lowering their standards because there is an outsized source of revenue. Would there be other kinds of lending institutions, for instance, BDCs that might be more inclined by their nature to be able and willing to take more credit risk because they recognize that coming out of the block with 20 percent of your credit risk in fees covers a lot of risk?

Mr. ROSENGREN. There are other types of organizations that provide loans in the market other than banks. This program is designed for depository organizations. In part, we want to be able to get this facility up and running quickly. In part, we have to make sure that BSA, AML, and Know Your Customer kinds of conditions are also met. So that is why this program has primarily been operated through the banking system.

Senator TOOMEY. Well, I see I am out of time, but I do want to follow up on the possibility that this kind of risk-return structure might be even better suited for other financial institutions. That is not to say that banks should not participate, but maybe we should broaden the universe of institutions that are permitted to participate.

Thanks, Mr. Chairman.

Mr. HILL. Thank you, Senator Toomey. We are going to do a second round now with Dr. Rosengren, and I will start that with 5 minutes. And as I start my second round, I want to ask unanimous consent to put two letters in the record: one from Senator Crapo dated July 31st with comments about the Main Street Lending Facility, and also a letter dated August 4th from Senators Loeffler, Cornyn, Braun, and Tillis on the Main Street. Not hearing any objection, those will be included in the record.

[The letters follow:]

Americans for Financial Reform Education Fund

August 12, 2020

Chairman Jay Powell
Board of Governors of the Federal Reserve System
20th St. and Constitution Ave. NW
Washington, DC 20551
ATTN: Staff of Main Street Lending Facilities

President Eric Rosengren
Federal Reserve Bank of Boston
600 Atlantic Avenue
Boston, MA 02210

Dear Chairman Powell and President Rosengren:

On behalf of the 17 undersigned organizations, we are writing concerning the application of the affiliation rules governing eligibility for loans from the Main Street Lending Programs (MSLP), which are only available due to the appropriation of public funds by Congress. These rules determine whether Main Street loans are limited to mid-size businesses or will become accessible to what are effectively much larger companies. We are particularly concerned about the possibility that weakening affiliation rules could provide inappropriate access to Main Street Lending Facilities for private equity owned companies, without requiring strict conditions to protect public funds from being diverted from their public purpose by the private equity owner.

As it stands, a majority owner of a company that collectively employs over 15,000 employees is ineligible for access to the Main Street Lending Program. For important public policy reasons, which the Federal Reserve is well aware of, this affiliation requirement blocks access by larger firms and should not include artificially un-affiliated portfolio firms of private equity companies.

While many businesses are struggling as a result of the pandemic, private equity backed businesses are distinct in that their business model is based on extreme leverage, often pushing the companies to operate on the very edge of bankruptcy to maximize the private equity owners' short term profits. Moreover, private equity firms are generally based on a wealth-extraction business model where the owners often divert funds from portfolio companies to the private equity fund or general partners, through dividend payments or in the form of monitoring or other fees charged to the company. Once diverted, such funds are not available for internal company purposes. Importantly, they will also not be available to pay back the loan, as the private equity firm is structured so the fund owners are bankruptcy remote from the portfolio companies.

Weakening the affiliation rule and making it easier for private equity firms to benefit from these programs – especially in the absence of strong conditions requiring worker retention, wage protection, investment in worker safety, or other public priorities – puts public funds at risk of supporting the private equity firms' partners while doing little if anything to preserve jobs or Main Street businesses.

In previous letters and comments our organizations have supported strong job retention and worker safety preconditions to any Federal Reserve assistance.[1] We continue to support such conditions and believe that they would achieve the public purpose of these programs while greatly reducing the likelihood of exploitation and abuse. In the specific case of affiliation rules and potential private equity access to the MSLP, we make the following additional recommendations:

- Maintain strong affiliation rules so that large private equity companies with access to capital markets financing (not to mention access to ample "dry powder") cannot take out loans for their portfolio companies.

- If private equity firms are allowed to access the public funds in the MSLP for their portfolio companies, require that loan proceeds be kept in the portfolio companies by banning dividends, monitoring fees, or any other form of transferring funds from the portfolio firm to the parent fund, general partner, or any other business or individual directly or indirectly affiliated with the parent fund or general partner. While dividends denominated as such are currently banned, other forms of transferring or draining value are not but should be.

- If private equity firms are allowed to access Main Street loans for portfolio companies, the Federal Reserve must require that the private equity fund be jointly liable with the portfolio firm for repaying the loan and for any other liability associated with the receipt or use of the proceeds of the loan. In the absence of such requirements, any funds moved from the portfolio company to the private equity parent will not be available to achieve the public purpose of the loan or to repay the public.

It is also important to take additional steps to make sure that the affiliation rules are properly enforced, including by ensuring that private equity owners do not use controlled shell companies to evade the majority ownership requirement of the affiliation rules. Many private equity backed companies which were not statutorily exempted from affiliation rules have been able to access the PPP program.[2]

We urge you to maintain strong affiliation rules in order to continue to focus the MSLP on genuine middle market companies, and, in the event that the Federal Reserve allows private equity firms to access the public funds made available in the program, to take steps to eliminate the ability of the parent fund to misuse or drain loan proceeds from the portfolio company and avoid liability for paying back the loan. Finally, we urge you, again, to impose meaningful conditions around retaining jobs, worker safety, or adequate protections against diversions to executives for all companies, including those that are owned or controlled by private equity firms. Thank you for your attention to these matters.

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[1] "Letter to Congressional Leadership on Conditions for Covid-Related Assistance", available at https://bit.ly/30QPK3V ; Americans for Financial Reform Education Fund, "Comment Letter to the Federal Reserve on April 9th Facilities", available at https://bit.ly/3gMOJzg .

[2] Louch, William, "Private Equity Firms Borrow from PPP Program, Despite Later Rules Barring Them", Wall Street Journal, July 7, 2020. Available at https://on.wsj.com/3iDodJo

Sincerely,

Action Center for Race and the Economy (ACRE)
AFL-CIO
American Economic Liberties Project
American Federation of State, County and Municipal Employees (AFSCME)
Americans for Financial Reform Education Fund
Better Markets
California Reinvestment Coalition
Center on Economic and Policy Research (CEPR)
Center for Popular Democracy (CPD)
Communications Workers of America
Consumer Federation of America
Private Equity Stakeholder Project
Project on Government Oversight (POGO)
Public Citizen
Strong Economy for All
Transform Finance
United for Respect

United States Senate
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
WASHINGTON, DC 20510–6075

July 31, 2020

The Honorable Steven T. Mnuchin
Secretary
Department of the Treasury
1500 Pennsylvania Avenue NW
Washington, DC 20220

The Honorable Jerome H. Powell
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Dear Secretary Mnuchin and Chairman Powell:

The Federal Reserve and Treasury Department recently announced that they would be extending various 13(3) emergency lending programs by three months, through December 31, 2020, in order to "facilitate planning by potential facility participants and provide certainty that the facilities will continue to be available to help the economy recover." There are also still funds available under section 4003(b)(4) of the CARES Act intended for Federal Reserve 13(3) facilities and I encourage the Federal Reserve and Treasury Department to quickly expand the Main Street Lending Program by setting up an asset-based lending program and commercial real estate program.

- Establishing a facility to accommodate asset-based lending could open access to critical resources for several industries that could not otherwise access the MSLP based on earnings or cash flow metrics. Such asset-based lending would be predicated on pledged collateral.

- Addressing the unique circumstances faced by commercial real estate, including securitized commercial mortgages, whether through access in the MSLP or a separate facility. Several options have been circulated and should be carefully considered in crafting the appropriate terms.

The Federal Reserve and Treasury have taken important steps to support the broader economy and I look forward to working with you both to continue to expand the Main Street Lending Program.

Sincerely,

Mike Crapo

Mike Crapo
Chairman

United States Senate
WASHINGTON, DC 20510-1010

August 4, 2020

The Honorable Steven T. Mnuchin
Secretary of the Treasury
U.S. Department of the Treasury
1500 Pennsylvania Avenue NW
Washington, D.C. 20220

The Honorable Jerome H. Powell
Chairman
Board of Governors of the Federal Reserve
20th Street and Constitution Avenue NW
Washington, D.C. 20551

Dear Secretary Mnuchin and Chairman Powell:

Thank you for your leadership of the Board of Governors of the Federal Reserve System (Fed) and the Department of the Treasury, and for the extraordinary, unprecedented steps you have taken in just four months to provide critically needed assistance to the U.S. economy. The Primary and Secondary Market Corporate Credit Facilities have restored pre-COVID liquidity in many asset classes, enabling larger companies with market access the ability to borrow capital to bridge over economic impacts of the pandemic and support American working families. Similarly, the Paycheck Protection Program has provided a lifeline to small businesses and spared the loss of millions of American jobs.

The programs for medium sized employers, however, have proven to be more challenging. We recognize that the Main Street Lending Program (MSLP), consisting of five credit facilities, offers to serve borrowers across industries with diverse collateral; no two borrowers' loans are exactly alike, and the assets are far less fungible than large companies' corporate bonds. In our view, the MSLP's success should be judged by the number of borrowers that are able to access the program (i.e., the take-up rate of the programs) and ultimately the number of jobs it saves. Judging by these standards, the MSLP has had a slow start, with only a handful of our nation's banks having signed up to be MSLP lenders and the issuance of only a few loans. In our judgment, more support to our nation's employers is needed. The MSLP is an untapped resource that has the potential to save thousands of jobs, but these could all be lost if businesses can't access the credit they need at this moment in time. As companies look to set 2021 budgets for hiring and capital expenditures, enhancements to the MSLP would give employers the certainty they need to maintain workers, hire, and invest in the coming year.

As Congress deliberates a new round of COVID-related relief, we encourage you to make full use of the tools available to the Treasury and the Federal Reserve in the CARES Act. While it is incumbent upon all of us in government to be good stewards of taxpayer dollars, we believe that the MSLP is far too restrictive to support employers and their employees through unprecedented economic hardship. The Exchange Stabilization Fund (ESF) is designed to backstop and provide stability in times of financial turmoil. Restricting the MSLP only to companies that can obtain financing outside of the program diminishes the usefulness of a program that Congress approved in March.

Based on feedback to our offices, middle-market companies are being turned away for a variety of reasons. Many banks seem disinterested in the program because they either wish to retain more than five percent of a profitable loan or they have no interest in retaining any stake at all in an unprofitable loan. Other banks are questioning the terms of the MSLP, such as the requirement that a loan be 200% collateralized in the Main Street Priority Loan Facility (MSPLF). And as a general matter, some are disinterested due to the complexities and reporting requirements.

We deeply respect your leadership and tenacity in the development of the MSLP and all of the recovery programs to stabilize our economy and workforce. But we also wish to convey—with urgency—our expectation that your agencies will take swift action to utilize the Title IV CARES Act credit support for small and medium sized employers. Below are views on how the program could be amended to better serve borrowers in our states and across the nation to save millions of American jobs.

- Reduce the minimum loan amount for the MSELF and MSPLF. The barrier to entry for small businesses is too great. We recommend lowering the minimum loan amount for those facilities, as the present minimum of $250,000 is overly restrictive and prevents small business access.

- Increase the maximum debt-to-EBITDA leverage ratio that qualifies borrowers for loans. While we continue to hear challenges faced by borrowers that currently qualify for a MSLP loan but cannot seem to get one, we also receive daily feedback from businesses in our state that do not qualify for the MSLP because of the leverage criteria. To be clear: we support the use of the MSLP to provide "rescue capital" to our economy. Businesses that were shut down by government orders and for which the MSLP is their only potential source of credit should not be allowed to fail for the sake of an unnecessarily restrictive CARES Act investment strategy. The MSLP should support cash flow-based lending to businesses that have strong earning potential, especially as the pandemic subsides, but which may not presently have any unencumbered collateral to offer; second-lien loans should also be considered. Businesses that were likely to fail before the shutdown should not be assisted, but businesses that were easily servicing their debt before the pandemic are quintessentially those the MSLP should be serving.

- Eliminate the 200% collateralization requirement in the MSPLF and increase the maximum loan amount. This facility offers loans to new borrowers (i.e., those without an existing facility with the lending bank) up to six-times 2019 EBITDA. Per the FAQs for the program, however, the maximum advance rate on a secured loan is limited to 50% because the program requires a 200% collateral coverage ratio. Many would-be borrowers have collateral to offer as security for which normal advance rate would be much higher than 50%. A prudent policy would be to require lenders to use their normal advance rates, which have been approved and continue to be monitored by their banking regulators. Additionally, the maximum loan amount should be increased to $300 million, setting it on par with the MSELF. Under current policy, if a borrower needs more than the $50 million available in the MSPLF and its existing lender does not want to extend it any new credit, the borrower cannot turn to another bank to seek a MSPLF loan. Increasing the MSPLF maximum loan size will encourage competition—and thus better terms—for borrowers.

- Provide greater incentives for lenders to participate in the MSLP. Currently, the only incentive for banks to participate appears to be in the Main Street Expanded Loan Facility (MSELF), where a bank with temporarily impaired collateral can have the Fed provide 95% of new credit to rehabilitate the business and, with it, the prior loan. Balance sheet support, which banks typically have no problem solving through syndication, seems to be the only incentive in the other two facilities. We suggest that the most effective solution is to eliminate the risk retention feature altogether and pay lenders a fee for originating loans according to Fed-provided underwriting criteria (much like the PPP's lender-as-distributor model). Alternatively, place the Special Purpose Vehicle's (SPV) resources in a first-loss position up to a certain percentage of credit loss rather than the current model of sharing losses *pari passu*. A third option is to allow lenders to collect more than 5% of the interest payable on the loan while retaining only 5% of the credit risk.

- Permit borrowers of MSLP loans to refinance debt within at least 12 months of the maturity period, revising the present prohibition on refinancing debt until it comes within 90 days of the maturity date. Business will need maximum flexibility during this crisis, and refinancing is a crucial tool in maintaining viability. Standard practice is to refinance debt 12-18 months before maturity; refinancing debt on a short schedule could create rollover risk and further imperil the financial health of businesses impacted by the pandemic.

Below are just a few examples of specific companies we have heard from that would benefit from the proposed changes outlined and better able to access capital to save jobs and invest in our economy through the lending facility:

- An oil and gas producer seeking a $130 million MSELF loan to maintain their employees and restart planned 2020 drilling programs.

- A fertilizer company seeking a $150 million MSELF loan to maintain and expand operations to help America's farmers.

- A COVID and Genomaic Testing Company seeking a $30 million loan to increase testing capacity to over a million tests per month and hire more workers.

In addition to these changes, we welcome your input on areas where the law may need to be changed to better serve businesses and their employees in our states. For example, structure MSLP loans at a lower interest rate than LIBOR+300 (note that the CARES Act envisioned a

Main Street facility at L+200, but Congress is aware of the "penalty rate of interest" language of the Federal Reserve Act). We welcome your constructive feedback on what changes, if any, may be needed to federal law to make the MSLP more effective and keep more employees on the job.

In closing, please be assured of our gratitude for your steady leadership during the COVID-19 pandemic. Our comments are offered in the hope that we can continue to have a constructive and productive approach to meeting the needs of small and medium-sized companies and saving millions of jobs in our states. If you have any questions, please do not hesitate to reach out to us directly.

Sincerely,

Kelly Loeffler
United States Senator

John Cornyn
United States Senator

Mike Braun
United States Senator

Thom Tillis
United States Senator

Mr. HILL. Dr. Rosengren, you have talked about you limited to depository institutions to get up and running quickly, and yet there are only 150 banks or so listed on the Fed's website thus far as registered lenders. And I cite that because in the emergency environment, right at the end of March and April, we were able to stand up the PPP program over in the CARES Act, and 5,400 banks swung into action in a patriotic way and in 7 days began distributing $520 billion and making 5 million PPP loans.

Granted, certainly the underwriting was very different. The mission was very different. I got that. But I am concerned about the reluctance of banks to participate in the program. Arkansas has 86 banks and yet only two banks headquartered in my State that are local banks have agreed to participate. So I really hope as we have this hearing today we will talk more about that.

Let me turn and talk about the term sheet. As you have noted, it is really a cash flow lending exercise based on a pre-tax, pre-depreciation, amortization multiple and implied leverage. In other words, it looks like a very traditional bank loan.

Where is the higher risk component that was contemplated in the CARES Act section that encourage help for particularly distressed sectors of the economy? Could you comment on that, Dr. Rosengren?

Mr. ROSENGREN. So I think these loans already are going to be risky. Doing lending in the middle of a pandemic, particularly if it is a sector of the economy where social distancing is difficult, so tourism, hotels, retail have all been badly affected by the pandemic. And some of those, as we have seen, there have been very large bankruptcies of retailers, for example. So these loans are not without risk, and I fully expect that some of the loans that we are going to do over time will have a loss. So that is why we have a Treasury backstop.

So I think this program has taken on a fair bit of risk. I think that over time, as the portfolio grows, we are going to have some significant losses. Hopefully that does not occur. Hopefully everybody is able to pay back the loan completely. But if the economy does not do well, particularly if the pandemic worsens, it is quite possible that we will experience significant losses.

Mr. HILL. Thank you——

Mr. ROSENGREN. So I expect that this program did focus on trying to get loans to fairly risky borrowers.

Mr. HILL. Thank you for that. But when you do look at the terms, I mean, you really are—I agree, companies at the margin are certainly middle-market companies that could not access the public markets or were not eligible for PPP, many would qualify here. But as I noted earlier, I think the affiliation rules make that more difficult. And I think the very traditional lending profile that is contained in this term sheet also could be a detriment to companies.

Let me give you an example, and this was talked about with Secretary Mnuchin and Chairman Powell at our meeting of a few weeks ago, and that is, someone who does not have good EBITDA in 2019, they certainly do not have it in 2020. But at the end of the year in 2019, they had very good collateral valuation. They had a low loan-to-cost potentially. They had a low loan-to-value potentially. They have room to lend, but they cannot meet the EBITDA standards. And both Jay Powell and Steve Mnuchin said they were "interested in looking at a collateral-dependent or asset-based loan."

Can you tell us what the status of that look is?

Mr. ROSENGREN. So the Main Street Program is a cash flow program. As a base financing——

Mr. HILL. But there are a lot of Main Street firms, Mr. President, that do not have cash flow in 2019, but they are absolutely a small middle-market type company. And so I know the Main Street term sheet is currently a cash flow. I am asking, is there current discussion underway to expand a different Main Street Facility that would be more of an asset-based loan rather than a cash flow loan?

Mr. ROSENGREN. I know there are discussions about asset-based financing and some of the difficulties experienced, for example, in commercial real estate. So there have been ongoing discussions about this, but there is no term sheet that is imminent.

Mr. HILL. Thank you for that.

Also, startup companies, truly people in the startup space have a disproportionate amount of costs. Are you looking at startups and what they might need in the Main Street arena?

Mr. ROSENGREN. Many times startups need equity more than they need debt, so I think frequently a true startup is going to find other types of financing vehicles more attractive. This is more of a program for established businesses that have experienced a disruption of cash flow.

Mr. HILL. Thank you, Mr. President.

Let me yield to my friend Mr. Ramamurti for 5 minutes.

Mr. RAMAMURTI. Thank you, Mr. Chairman.

In early April, the Fed announced the first version of the Main Street Lending Program. That announcement described certain basic features of the program like the maximum loan amount and the rates and terms for loans.

A few weeks later, the Fed announced major changes to the program. Many of those changes lined up exactly with what members of the oil and gas industry had requested. That did not appear to be a coincidence. Shortly before the changes were announced, President Trump publicly promised that oil and gas companies would be taken care of. And then shortly after the changes were announced, the Energy Secretary went on TV and bragged about how he and Treasury Secretary Mnuchin had succeeded in getting the Fed to make changes that the oil and gas industry wanted.

But when asked by reporters, a spokesperson for the Fed denied that the Fed had made any adjustments out of consideration for the oil and gas industry. Instead, the Fed said that the April changes reflected the more than 2,000 public comments that the Fed had received about the initial design of the program.

So, President Rosengren, as the Regional Fed President responsible for the Main Street Program, do you stand by the Fed's earlier statement that certain adjustments were not made specifically to help oil and gas companies?

Mr. ROSENGREN. I do. This is a broad-based program. It has been a broad-based program from the start. 13(3) facilities require broad-based kinds of terms, and so it is not targeted at specific firms or specific industries. 13(3) facilities are not available for that kind of lending.

Mr. RAMAMURTI. Thank you. And, look, I want to focus specifically on the changes that were made to the facility in April. Let us look at one of them. According to Reuters, in mid-April one of the key changes the Energy Secretary and Treasury Secretary were pushing for to help the oil and gas industry was increasing the maximum loan amount to at least $200 million. A couple of weeks later, when the Fed announced its changes to the Main Street Program, the maximum loan amount had gone up to exactly $200 million.

President Rosengren, out of the more than 2,000 public comments that were submitted to the Fed on the Main Street Program, are you aware of a single one that requested increasing the maximum loan amount to $200 million?

Mr. ROSENGREN. We got many comments from both banks and businesses that if the loan amount was larger, that it would be a more attractive facility for them. Remember, a lot of this discussion was occurring in March and April. The economic conditions and the pandemic conditions were very different at that time, and there was a lot of concern that some fairly large businesses would have difficulty getting financing.

Fortunately, the pandemic subsided, at least for a couple months, and as a result, many of those large borrowers that thought that they were going to need the financing at least to date have not actually accessed the program. I would highlight—

Mr. RAMAMURTI. Thank you. Just in the interest of time, I want to move on because, look, I reviewed each and every one of those 2,000-plus comments, and there was not a single one that requested specifically a $200 million maximum loan amount. The only people making that request were the Energy Secretary and the Treasury Secretary after meetings with the oil and gas industry.

Here is another change. The first version of the Main Street Program required companies to say in writing that they needed the loan "due to the exigent circumstances presented by the COVID–19 pandemic." Advocates for the oil and gas industry pushed to eliminate that requirement, presumably because many oil and gas firms were struggling before COVID and could not satisfy the requirement. And, again, in the final version, the Fed eliminated that requirement.

President Rosengren, again, out of the more than 2,000 public comments that the Fed received, are you aware of a single one outside the oil and gas industry that requested that the Fed remove this important requirement?

Mr. ROSENGREN. In the discussions I have been involved in, we do not discuss specific industries. We discuss how we can provide a broad-based financing scheme.

Mr. RAMAMURTI. Okay. I appreciate that. But, again, I reviewed the public comments, and there was not a single one that requested this change. Only the oil and gas lobby had requested it.

So I just want to ask one more time. Despite evidence that President Trump wanted oil and gas companies to get Federal relief, that the Energy Secretary and the Treasury Secretary pushed the

Fed for specific changes to accommodate the oil and gas industry, and that the Fed made changes that the oil and gas industry requested but no other industry or group requested, is it still your position that the Fed did not make certain changes to accommodate the oil and gas industry?

Mr. ROSENGREN. It is my position that the focus has been a broad-based lending program, not focused on any particular industry.

Mr. RAMAMURTI. Okay. Look, I think that, again, my focus is on specifically the changes that were made, not the overall scope of the program. And I think the evidence here is strong and deeply concerning. This is just not how the Fed is supposed to operate. The Fed is not supposed to be changing the rules of these programs so that the President's favorite companies can get access to billions of dollars in public money. In fact, it is illegal for the Fed to structure these lending programs to help specific companies avoid bankruptcy.

I urge this Commission to further investigate this issue, including by requesting all communications on this topic between the Fed and the Energy Secretary, the Treasury Secretary, and any representatives of the oil and gas industry.

Thank you, Mr. Chairman.

Mr. HILL. Thank you. The gentleman yields back.

Congresswoman Shalala is recognized for 5 minutes.

Ms. SHALALA. Thank you. My colleague is appropriately asking why the loan is as big as it is. I am actually interested in why it is not smaller.

Commentators have speculated the minimum loan amount of \$250,000 is too large and precludes participation by many small and mid-sized businesses. I am aware that the Fed has already reduced the minimum loan amount down from \$1 million to \$250,000, which may still be too high. For instance, the American Bankers Association and the Marketplace Lending Association have separately suggested that \$50,000 may be a more appropriate amount.

Has the Fed conducted studies on whether the \$250,000 loan minimum excludes parts of the market that this program is supposed to help? What changes can be made to make the program more broadly acceptable and accessible?

Mr. ROSENGREN. So for many of those smaller businesses, the PPP program was designed to target that segment of the industry. The PPP program is much more attractive to a small business because it has the ability to be a grant. So this program was really designed for businesses that did not qualify for the PPP program and, nonetheless, might have a need for credit.

So if you look at the actual loans that are in our portal, just the loans that are actually in the portal is \$1 to \$5 million. That is, the type of loan that we are seeing is dental companies, construction companies, design companies, retailers. These are businesses that frequently are going to have a \$1 to \$5 million loan, and it is not surprising that that is what we are actually seeing.

Now, we have seen some loans that are much bigger. We have seen some loans that are much smaller. But I would say that so far has been where we have seen the bulk of the activity.

Ms. SHALALA. So you are not considering going below $250,000?

Mr. ROSENGREN. I think there are probably other programs that are better designed, so a real question is whether a cash flow lending program such as Main Street is appropriate for very small businesses and whether there might be better targeted tools that can address that.

In particular, will more debt help that small business, or might it push it towards bankruptcy and closure? So we want to make sure that we provide debt to businesses that can use it and actually pay it back. We do not want to give businesses so much debt that they are not able to survive.

Ms. SHALALA. Thank you. Let me talk about the nonprofit organizations. A few weeks ago, you expanded the Main Street Lending Program to nonprofit organizations. Although these facilities are not yet live, I am concerned that the program requirements are too rigorous and will preclude participation by many of the nonprofits that need credit to survive the pandemic.

For example, the minimum loan size is $250,000, which may be too large for many smaller organizations. Borrowers are also required to have at least 60 percent of their expenses covered by nondonation revenue, which can be very hard for many nonprofits to achieve.

Can you talk about why the program was designed this way? I am very familiar with nonprofits, and that 60-percent requirement seems to me will block many nonprofits. I would appreciate hearing about any analysis that the Fed has done regarding the nonprofit interest and eligibility in the program. Have you considered changing any of the eligibility requirements? And, lastly, when do you expect the program to be launched?

Mr. ROSENGREN. So in terms of the nonprofit term sheet, when the first term sheet came out, we got extensive comments from a wide variety of nonprofits and a wide variety of banks. Many banks actually do not lend to nonprofits because it is a very different nature. Many of the large nonprofits—the University of Wisconsin, which you used to be associated with, probably goes to debt markets rather than relying primarily on bank markets. That is true for many hospitals as well.

So this is a market that has not been extensively tapped by many banks, and I think it is a new market for many banks. I think there is an opportunity for more nonprofits to be able to access bank financing through this program. We did make significant adjustments in the term sheet. When we were thinking about the term sheet and the adjustments we made between the first and the second term sheet, we spent an extensive amount of outreach understanding how banks underwrote these loans and how rating agencies underwrote these loans. These criteria broadly match what many of the banks told us the criteria was that they used. And between the first and second term sheet, we did relax it in response to the comment that it was being too restrictive.

In terms of when this facility is going to be up, we just got the legal documents up. The term sheet is now finished. We are in the process of doing the programming now. It is going to probably take us another several weeks before it is up and running. But I would highlight that now that the legal—bank loans do not get made quickly. So now that the legal documents are up and running, now that the term sheet is widely available, banks can start the negotiation with nonprofits about what facility is available. They are able to quickly submit it to the facility and get it funded.

So because of the long lags in making these kinds of agreements——

Mr. HILL. Thank you, Doctor.

Mr. ROSENGREN [continuing]. I think that this will be about the time that if a bank was going to do a nonprofit loan, that we will probably be up and running around the time that they complete the agreement with the borrower.

Mr. HILL. Thank you, Dr. Rosengren. The gentlewoman's time has expired.

Senator Toomey.

Senator TOOMEY. Thanks, Mr. Chairman.

Dr. Rosengren, I would like just to have final clarity on this. Just answer this, if you would. Is there any Main Street Lending Program that is available only to the oil and gas sector?

Mr. ROSENGREN. No.

Senator TOOMEY. And is there any program the terms of which are suitable only to the oil and gas sector?

Mr. RAMAMURTI. No.

Senator TOOMEY. Thank you.

I want to underscore a point that Congressman Hill raised, which is some real challenges with the affiliation rule, firms that, when we were drafting this legislation, we did not think would be automatically excluded from financing. I also want to underscore his point about considering asset-based facilities. I think you are very well aware there are some real challenges in the commercial mortgage-backed security market right now. In particular, the hotel subset of the commercial mortgage-backed sector is experiencing some real difficulties. And because they generally do not qualify for the EBITDA criteria, there is no access to this. As you know, the problem is exacerbated by the obligation of the servicers to go on and make payments, you know, irrespective of the ability of the borrower to do so.

So I would like to encourage you, as I have encouraged Secretary Mnuchin and Chairman Powell, to consider whether there should not be an asset-based category if there is an appropriate loan-to-value, that maybe that is a criteria that we ought to consider. Do you have any thoughts on whether we ought to stand up a facility specifically designed—it would be designed generally for the broad category of real estate, I think, and other categories that would be more suitable for an asset-based lending than they are for an EBITDA constraint?

Mr. RAMAMURTI. Yes, so an asset-based program would differ from what we have for Main Street, so it would be a different facility if it was done through a facility. Most of that type of lending has a much longer maturity than 5 years, so as you know, these are 5-year loans with a balloon payment at the end of the 5 years. That is probably not appropriate, for example, for retail or commercial real estate such as hotels.

So the nature of that program would be quite different. I know there is work being done thinking about how asset-based can be addressed, including through the SBA. So I think there are a number of proposals that are being considered. I am certainly aware that there are many concerns in the commercial real estate industry, and those concerns will get even worse if the pandemic gets worse.

Senator TOOMEY. Okay. So I want to go back to that. On page 11 of your testimony, you indicated that you believe that should the pandemic and the economic circumstances worsen, we might very well see greater interest in the Main Street Lending Programs. And I can certainly understand that leading to greater demand on the corporate borrower side. But could you address why you believe that that would not be offset by greater reluctance on the part of banks to take on the exposure in that scenario in which the environment worsens?

Mr. ROSENGREN. So there are many borrowers who could take 2 or 3 months of disrupted cash flow, and if it was only 2 or 3 months, those may be bankable loans right now, and they might be able to get a rate that is better than LIBOR plus 300 basis points.

However, if we go through another 3 months so that in 1 year's time they have experienced 6 months of badly disrupted cash flow, some of those loans that might have been attractive to get direct financing from the bank through the standard bank-borrower relationship may no longer be possible, and the bank may only be willing to do it if the Federal Reserve takes the 95-percent stake that is part of this Main Street Program.

So I agree with you that risk aversion by banks may increase if the pandemic gets worse, and there already is very substantial uncertainty. But many borrowers that cannot get access from their banks are going to be looking to the Main Street Program to provide that type of financing.

Senator TOOMEY. Thank you very much.

Thank you, Mr. Chairman.

Mr. HILL. The gentleman yields back. Thank you, Mr. Toomey.

And now we will hear from Ms. Anderson on our second—well, first let me thank Dr. Rosengren from his testimony today. We very much appreciate your written testimony and the interaction with our Commissioners.

And now let us turn to our second panel. We are going to hear from Ms. Anderson with the Bank Policy Institute first. Ms. Anderson, you are recognized for 5 minutes.

STATEMENT OF LAUREN ANDERSON, SENIOR VICE PRESIDENT AND ASSOCIATE GENERAL COUNSEL, BANK POLICY INSTITUTE

Ms. ANDERSON. Thank you. Members of the Commission, my name is Lauren Anderson, and I am a senior vice president and associate general counsel at the Bank Policy Institute. I thank you for the opportunity to be a witness at today's hearing regarding the Main Street Lending Program. BPI is a nonpartisan public policy, research, and advocacy group, representing the Nation's leading banks. Our members employ nearly 2 million Americans, make 72 percent of all loans and nearly half of the Nation's small business loans. BPI strongly supports the efforts to date as well as ongoing efforts by Congress, the Treasury, and the Federal Reserve to tackle the COVID crisis and provide much needed relief to households and businesses.

At the outset, it is worth noting how unique the Main Street Program is in relation to emergency lending programs established during the pandemic—or even in 2008 and 2009. It is not a loan forgiveness or grant program like the PPP, and it is not a market liquidity program for debt of investment grade borrowers. Main Street requires credit underwriting decisions on a heterogeneous set of individual nonbank borrowers, which is challenging and not something the Federal Reserve has done before. With the expansion of Main Street to nonprofit organizations, which themselves are very different across different sectors, the Federal Reserve ventured even further into unchartered territory. BPI, working with commercial lending experts from our member banks, has been actively engaged in commenting on the program since the initial term sheets were published in early April and through subsequent iterations.

The focus of our comments has largely been on ensuring the terms of the program are consistent with market practices and ensuring prudent risk management to safeguard taxpayer funds. We commend the Federal Reserve for seeking public comment on the terms of the program and engaging in an iterative process to try to improve the end result.

We are very pleased that the program began accepting lender registration in June and officially became operational on July 6. Since then, lenders continue to register, and loans, albeit a small amount, are being made. Many BPI member banks have registered and are in the process of reviewing borrower inquiries. While the limited number of loans made thus far has been a concern to some, it must be assessed in the context of a larger commercial credit ecosystem.

First, for many small businesses, Main Street may not be the right fit given the complexity of the program and the compliance requirements. However, BPI member banks helped to provide over 1.6 million PPP loans totaling over $188 billion to help small businesses meet payroll needs.

Second, larger corporates retain access to capital markets, which remain extremely active with the support of numerous Federal Reserve programs. Investment grade debt and corporate debt has been issued at record levels, with U.S. companies raising over $1 trillion year to date.

Third, and perhaps most significantly, over the course of March and April, both small and large businesses drew down on existing credit lines. Between February 12 and April 1, bank loans increased by approximately $700 billion. Thus, the lack of demand for Main Street loans likely indicates that many other eligible businesses are finding credit through other market channels.

A second reason why there is limited demand for Main Street, the fact that the program not only requires borrowers to meet certain eligibility criteria, but also to satisfy bank underwriting standards. And if a borrower can meet bank underwriting standards, it is not surprising that they are finding credit solutions through traditional market channels. Where the Main Street Program may become more useful is if banks become balance sheet constrained and cannot lend the full amount needed by a creditworthy borrower. If there were to occur, Main Street may provide the solution. But so far bank balance sheets are robust in weathering the crisis. If, however, Congress, the Treasury, or the Federal Reserve desires to provide further relief to small and mid-sized businesses experiencing acute stress due to the pandemic, including less creditworthy borrowers who would not currently pass bank underwriting standards, the design of the program would need to be modified. At the moment the program is not designed to provide loans to less than creditworthy borrowers. If banks are to provide loans to borrowers who cannot meet current bank underwriting standards, the Government would need to provide downside credit risk protection that would allow Main Street loans to be considered lower risk.

I thank you again for the opportunity to be a witness for the Commission, and I look forward to answering your questions. Thank you very much.

[The prepared statement of Ms. Anderson follows:]

Lauren Anderson, Senior Vice President and Associate General Counsel, The Bank Policy Institute

Testimony before the Congressional Oversight Commission

"Hearing to Examine the Main Street Lending Program"

August 7, 2020

Members of the Commission, my name is Lauren Anderson and I am a Senior Vice President and Associate General Counsel at the Bank Policy Institute (BPI). I thank you for the opportunity to be a witness at today's hearing regarding the Main Street Lending Program (MSLP). BPI is a nonpartisan public policy, research and advocacy group, representing the nation's leading banks. Our members include universal banks, regional banks and the major foreign banks doing business in the United States. Collectively, they employ nearly 2 million Americans, make 72% of all loans and nearly half of the nation's small business loans and serve as an engine for financial innovation and economic growth. BPI strongly supports the efforts to date by Congress, the Treasury and the Federal Reserve to tackle the COVID crisis and provide much needed relief to households and businesses.

On March 23, 2020, the Federal Reserve announced that it would be establishing a Main Street Business Lending Program;[1] and, as part of Title IV of the CARES Act, Congress shortly thereafter provided $454 billion to be used to support loan and loan guarantees provided by Federal Reserve lending facilities, including the MSLP. On April 9, 2020, the Federal Reserve announced the first iteration of the term sheets for the MSLP and indicated that it would be able to purchase up to $600 billion in loans supported by $75 billion in equity provided by Treasury through the Exchange Stabilization Fund (ESF).[2] Last week, the Federal Reserve announced that it would be extending the scheduled expiration of its emergency lending programs, including the MSLP, from September 30 through the end of the year.[3] BPI, working with commercial lending experts from its member banks, has been actively engaged in commenting on the MSLP since these initial term sheets were published in early April and through subsequent iterations, including the newly added facilities related to nonprofit organizations.

At the outset, it is worth noting how unique the MSLP is in relation to emergency lending programs established during the pandemic--and even in relation to emergency programs established during the financial crisis in 2008 and 2009. This program is not a loan forgiveness or grant program like the Paycheck Protection Program, and it is not a market liquidity program for debt of investment grade borrowers. The MSLP requires credit underwriting decisions on a heterogeneous set of individual non-bank borrowers, which is challenging and not something the Federal Reserve has done before. With the expansion of the MSLP to nonprofit organizations, which themselves are very different across different sectors, the Federal Reserve ventured even further into unchartered territory. Given the complexity of the task and the need to complete it as soon as possible, it was entirely sensible for the Federal Reserve

[1] *See* "Federal Reserve announces extensive new measures to support the economy," (March 23, 2020); *available at* https://www.federalreserve.gov/newsevents/pressreleases/monetary20200323b.htm
[2] *See* "Federal Reserve takes additional actions to provide up to $2.3 trillion in loans to support the economy," (April 9, 2020); *available at* https://www.federalreserve.gov/newsevents/pressreleases/monetary20200409a.htm
[3] *See* "Federal Reserve Board announces an extension through December 31 of its lending facilities that were scheduled to expire on or around September 30," (July 28, 2020); *available at* https://www.federalreserve.gov/newsevents/pressreleases/monetary20200728a.htm

to leverage the expertise of banks in making lending decisions and to seek comment from lenders to establish the terms of the program.

The focus of BPI's comments to date has largely been on ensuring the terms of the program are consistent with market practices, so the program can quickly achieve the broadest participation possible, and ensuring prudent risk management to safeguard taxpayer funds. We commend the Federal Reserve for seeking public comment on the terms of the program and engaging in an iterative process to try to improve the end result. For example, we welcomed the adjustments to the original term sheets with regard to the definition of EBITDA, the move from SOFR to LIBOR and the more recent adjustments to lengthen loan tenure from 4 to 5 years and allow for co-borrowers.

We are very pleased that the program began accepting lender registration in June[4] and officially became operational for business lending and to purchase participations in eligible loans on July 6.[5] Since then, lenders continue to register and loans, albeit a small amount, are being made. According to testimony from Federal Reserve Chairman Powell in front of the House Financial Services Committee at the end of June, over 300 lenders had begun the process of registering[6]. A number of BPI member banks have registered; and 11 BPI members have indicated that they will be accepting applications from new customers.[7] As of July 29, the Federal Reserve had purchased $82 million in participations of Main Street Loans.[8]

The limited number of loans made thus far under the MSLP can best be understood by recognizing its place in a larger commercial credit ecosystem. First, many smaller businesses that received PPP loans, and eventually grants, did not require MSLP loans in addition. BPI member banks for instance helped provide over 1.6 million PPP loans totaling over $188 billion to help small businesses meet payroll needs.[9] Second, the largest businesses retain access to capital markets, which remain extremely active with the support of numerous Federal Reserve programs. Investment grade and corporate debt has been issued at record levels, with U.S. companies raising over $1 trillion year to date. Third, and perhaps most significantly, as the severity of the health crisis became evident in the first quarter, both small and large businesses prudently accessed credit from their banks to ensure liquidity. Between February 12, 2020 and April 1, bank loans increased approximately $700 billion, in large part because banks were funding draws on lines of credit as large and small businesses sought to stockpile

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[4] *See* "Federal Reserve's Main Street Lending Program opens for lender registration," (June 15, 2020); *available at* https://www.bostonfed.org/news-and-events/press-releases/2020/federal-reserves-main-street-lending-program-opens-for-lender-registration.aspx

[5] *See* "Boston Fed announces Main Street Lending Program is fully operational," (July 6, 2020); *available at* (https://www.bostonfed.org/news-and-events/press-releases/2020/boston-fed-announces-main-street-lending-program-is-fully-operational.aspx

[6] *See* Testimony of Chairman Jay Powell before the House Financial Services Committee "Oversight of the Treasury Department's and Federal Reserve's Pandemic Response," (June 30, 2020); *available at* https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=406688

[7] Information retrieved on August 4, 2020 from https://www.bostonfed.org/supervision-and-regulation/supervision/special-facilities/main-street-lending-program/information-for-borrowers.aspx#map

[8] Information retrieved on August 4, 2020 from https://www.federalreserve.gov/releases/h41/current/h41.htm

[9] *See* "Paycheck Protection Program (PPP) Report," (July 31, 2020); *available at* https://home.treasury.gov/system/files/136/SBA-Paycheck-Protection-Program-Loan-Report-Round2.pdf

cash.[10] Thus, a lack of demand for MSLP loans likely indicates that most businesses are finding credit through other market channels.

Given the fact that the MSLP requires borrowers to not only meet certain eligibility criteria, but also to satisfy bank underwriting standards, it is not surprising that creditworthy borrowers are finding solutions through normal market channels: borrowers generally prefer to avoid the stigma of government assistance if private sector funding is available, and lenders have incentives to continue serving creditworthy borrowers. Where the MSLP may be more useful is where a bank is balance sheet constrained and cannot lend the full amount needed by a creditworthy borrower. In this instance, an MSLP loan may be attractive to both a borrower and a lender as the MSLP SPV will buy 95% of the loan through the participation structure. However, as demonstrated by the Federal Reserve's recent stress test in which nearly all banks were projected to remain well capitalized even in a severe further downturn, banks currently have plenty of capital to support their lending. In this regard, we believe the MSLP may be of greater utility if the economic downturn worsens and banks come under greater pressure.

If, however, Congress desires to provide further relief to small and midsize businesses experiencing acute stress due to the pandemic, including less creditworthy borrowers who would not currently pass bank underwriting standards, the design of the program would need to be modified. MSLP loans originated as "non-pass" credits would be classified by bank examiners and treated as workouts; non-pass credits would also likely trigger examiner criticism, higher capital charges, and other regulatory constraints. Furthermore, the additional leverage created by an MSLP loan might cause a downgrade of an existing bank credit. So, even a 5 percent participation in an MSLP loan to a borrower that is anything but creditworthy carries significant disincentives for a bank to participate. To avoid this outcome, the government would need to provide downside credit risk protection that would allow the MSLP loan, and existing credit, to be considered lower risk.

I thank you again for the opportunity to be a witness for the Commission and I look forward to answering your questions.

[10] Recent regulatory reports and banks' earnings reports indicate that many of the recent draws on credit lines have been repaid.

BANK POLICY INSTITUTE

August 31, 2020

Via Electronic Mail

Commissioner Ramamurti
Congressional Oversight Commission

Re: **Follow-up Question from Hearing on August 7, 2020 Examination of the Main Street Lending Program Established by the Federal Reserve Pursuant to the CARES Act**

Dear Commissioner Ramamurti:

The Bank Policy Institute appreciated the opportunity to be a witness before the Commission on August 7, 2020 and we thank you for your follow-up question and continued engagement regarding the Main Street Lending Program (MSLP). With regard to your specific question, please find our response below.

I. **Do lenders collect demographic data on borrowers in the absence of federal program mandate to collect and report such data? If not, will BPI commit to working with its members to collect such demographic data for MSLP loans?**

BPI is not specifically aware of BPI member banks collecting demographic data on MSLP applicants or MSLP borrowers who ultimately receive funds under the Program.

Given BPI member banks represent less than 10% of registered lenders it may be more appropriate for such data to be systematically collected by the Federal Reserve Bank of Boston to get a more accurate picture of loan distribution across demographics. BPI member banks would of course be willing to work with the Federal Reserve Bank of Boston to determine how best to capture such data through the portal process.

Alongside working with the Federal Reserve Board, the Federal Reserve Bank of Boston and the Treasury to ensure the MSLP is reaching LMI communities and minority-owned businesses, BPI banks are very committed to serving such communities and businesses. For example, about four-in-ten PPP loans originated by large banks went to businesses in low- to moderate-income or predominantly minority areas, according to a recent BPI survey of its largest member banks.[1] Additionally, BPI members are partnering with Community Development Financial Institutions and Minority Depository Institutions to better support financial inclusion and minority entrepreneurship and success. As a result, BPI is supportive of efforts in Congress to expand investments in CDFIs and MDIs, including legislation that would provide long term equity to these institutions to deliver further support to underserved borrowers and borrowers in minority communities.

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Bank Policy Institute appreciates the opportunity to engage with the Commission. If you have any questions, please contact the undersigned by phone at 202-737-3536 or by email at Lauren.Anderson*@bpi.com.*

Respectfully submitted,

Lauren Anderson
Senior Vice President and Associate General Counsel
Bank Policy Institute

[1] *See* "Large Banks Are Serving the Credit Needs of Small Businesses in Low- and Moderate-Income and Minority Communities Through the Paycheck Protection Program," (June 22, 2020); *available at* https://bpi.com/press-releases/large-banks-are-serving-the-credit-needs-of-small-businesses-in-low-and-moderate-income-and-minority-communities-through-the-paycheck-protection-program/

Mr. HILL. Thank you, Ms. Anderson. We appreciate your testimony.

We will now turn to Mr. Bohn. You are recognized for 5 minutes.

STATEMENT OF THOMAS BOHN, PRESIDENT AND CHIEF EXECUTIVE OFFICER, ASSOCIATION FOR CORPORATE GROWTH

Mr. BOHN. Well, thank you. Good morning, and thank you for the invitation to speak today.

Congressman Hill, Commissioner Ramamurti, Congresswoman Shalala, and Senator Toomey, I appreciate the gravity of the responsibility before you, admire your willingness, and respect your commitment to ensure that Federal relief programs enacted through the Coronavirus Aid, Relief, and Economic Security Act are both accessible and effective.

I am here this morning to provide testimony from the perspective of middle-market borrowers to help answer the question that you all are asking of who the Main Street Lending program is helping. Regrettably, I have no answer to offer you. We could neither borrow from the program nor find someone in our membership who has received a loan through it.

To help illustrate the current obstacles to securing loans through MSLP, I would like to share some comments from our members who completed a survey administered in recent days. I will not read all of them. These are their words, not mine:

The program is moving too slowly, whereas COVID–19 dramatically and quickly caused an impact.

We actively solicited a MSLP loan for a Minority Business Enterprise, a company whose performance is only 10 to 15 percent lower during the pandemic as it was beforehand. We approached 15 lenders. Not one was interested.

If the MSLP applies to the lower middle market, it is news to me. If it does, please send guidelines.

We were excited about the program initially and had two companies that would be perfect for the program, but the banks will not do it.

We had plenty more comments that address the challenges faced by both borrowers and lenders which I am happy to provide the Commission for its review and reporting purposes.

As the CEO and president of the Association for Corporate Growth, ACG, I come before you today as an employer and the leader of an association that represents a vitally important segment of the economy which employed some 45 million Americans prior to the pandemic. Founded in 1954, ACG's 15,000 members operate, advise, and grow approximately 200,000 middle-market companies.

As a networking organization which hosted more than 1,100 live events annually, ACG, like many other associations, was devastated by COVID. I lead a staff of nearly 30 people based out of Chicago, or now all over the country, as well as oversee operations in 60 chapters, primarily in North America. When the Paycheck Protection Program was announced, a grant through it would have served as an $800,000 lifeline for my Chicago team and staff members dispersed throughout the country. However, as a 501(c)(6), we too were ineligible.

Consequently, we made more than $600,000 in salary cuts—currently forecasted to continue through December and beyond. Since March, every conversation with our members finds them in the same position—with their employees at the forefront of their operations, they managed cash flow, tried to prevent layoffs, and worked diligently to retain employees and not lose institutional knowledge.

When PPP was closed to us, like many other associations and a large percentage of our member companies, we looked in earnest at the Main Street Lending Program. A loan would allow us to invest in the digital enhancements to our infrastructure that would ensure we could continue to deliver strong member value and the necessary tools for business development in this new virtual world.

But there, too, we found another closed door, as did our members. Perhaps naively, we thought the Main Street Lending Program would be accessible to organizations and companies excluded from the PPP. Suffice to say it has not been accessed by many. In your recent report, you talked about the Goldman Sachs estimating that some 45 million Americans or 40 percent of private-sector are employed by companies who are eligible for MSLP, yet very few had purchased a loan. Further, Chairman Powell recognized the challenges with the small and medium-sized businesses for which MSLP is intended. It is new territory for the Federal Reserve and very complex because these businesses are a "broad and heterogeneous class of borrowers'" with diverse needs.

In our opinion, the challenges with the Main Street Lending Program are twofold and equate to awareness and access.

Our recent survey found 22 percent of the respondents completely unaware of MSLP. And of the respondents who want to apply for the loans through the program, 81 percent were unable. When asked what changes could help, they suggested the removal or the overhaul of the following items, which some of you have talked about today:

Removal of adherence to the SBA affiliate definition. We talked about the EBITDA/leverage size based test which excludes many companies, particularly those early in their life cycle and family-owned businesses; distribution dividends restrictions for 1 year after loan payoff; employee compensation restrictions for 1 year after loan payoff; decreasing the minimum loan size.

Look, creating a greater awareness of the MSLP and increasing accessibility should result in a groundswell of applicants. We believe that. The effect should help companies retain jobs and maintain operations, and consequently preserve health care insurance for millions of Americans in this increasingly unpredictable economy tethered to COVID 19.

We stand to support you in any way you need and hope to answer any questions you may have today. Thank you.

[The prepared statement of Mr. Bohn follows:]

August 7, 2020 Testimony before the CARES Congressional Oversight Commission
Thomas Bohn, President and CEO
Association for Corporate Growth
125 S. Wacker, Suite 3100
Chicago, IL 60606

Good morning,

Thank you for the invitation to speak to you today.

Congressman Hill, Commissioner Ramamurti, Congresswoman Shalala and Senator Toomey, I appreciate the gravity of the responsibility before you, admire your willingness and respect your commitment to ensure that federal relief programs enacted through the Coronavirus Aid, Relief, and Economic Security Act are both accessible and effective.

I am here this morning to provide testimony from the perspective of a borrower. To answer the question of who the Main Street Lending program is helping? I have no answer to offer you. Regrettably, I could neither borrow from the program nor find someone who has received a loan through it.

To help illustrate the current obstacles to securing loans through the Main Street Lending Program, I'd like to share comments from our members who completed a survey administered in recent days. These are their words:

- *The program is moving too slowly, whereas COVID-19 dramatically and quickly caused impact.*
- *The government created a fire hydrant to get money flowing into the economy. Commercial banks are tepidly attaching garden hoses to the fire hydrants.*
- *We actively solicited a MSLP loan for a Minority Business Enterprise, a company whose performance is only 10-15% lower during the pandemic as it was beforehand. We approached 15 lenders. Not one was interested.*
- *If the MSLP applies to the lower middle market, it is news to me. If it does, please send guidelines.*
- *We were excited about the program initially and had two companies that would be perfect for the program, but the banks won't do it.*
- *We have talked with 12 national and regional banks who are approved MSLP lenders but do not want to provide credit to any of our companies under the program due to the construct and underwriting risks of the program.*
- *Banks are holding back applications using their own very restrictive criteria. Availability must be able to address firms who are distressed due to COVID.*

I have plenty more comments that address the challenges faced by both borrowers and lenders, which I am happy to provide to the commission for its review and reporting purposes.

As the CEO and President of the Association for Corporate Growth (ACG), I come before you today as an employer and the leader of an association that represents a vitally important segment of the economy which employed some 45 million Americans prior to the pandemic. Founded in 1954, ACG's 15,000 members operate, advise, and grow 200,000 middle market companies.

As a networking organization which hosted more than 1,100 live events annually, ACG, like many other associations was devastated by COVID. I lead a staff of 23 people based out of Chicago, as well as oversee operations in 60 chapters, primarily in North America. When the Paycheck Protection was announced, a grant through it would have served as an $800,000 lifeline for my Chicago team and staff members dispersed throughout the country.

However, as a 501c6, we were ineligible.

Consequently, we made more than $600,000 salary cuts – currently forecasted to continue through December. Since March, every conversation with our members finds them in the same position - with their employees at the forefront of their operations, they managed cash flow, tried to prevent layoffs, and worked diligently to retain employees and not lose irreplaceable institutional knowledge.

When PPP was closed to us, like many other associations and a large percentage of our members' companies, we looked in earnest at the Main Street Lending Program. A loan would allow us to invest in the digital enhancements to our infrastructure that would ensure we continue to deliver strong member value, and the necessary tools for business development in a virtual world.

But there, we found another door closed. Sadly, our experience greatly mirrored ACG's members.

Perhaps, naively we thought the Main Street Lending Program would be accessible to organizations and companies excluded from the PPP? Suffice to say it hasn't been accessed by many. In your most recent report, [1] Goldman Sachs estimated that some 45 million Americans, or 40% of private sector workers are employed by a company eligible for the MSLP, yet, a single $12 million loan had been purchased. Further, Chairman Powell recognized the challenges with the small and medium-sized businesses for which MSLP is intended; it is new territory for the Federal Reserve and very complex because these businesses are a "broad and heterogeneous class of borrowers" with diverse needs.

In our opinion, the challenges with the Main Street Lending Program are two-fold and equate to awareness and access.

[1] The Third Report of the Congressional Oversight Commission, https://coc.senate.gov/sites/default/files/2020-08/20200720_Congressional_Oversight_Commission_3rd_Report.pdf

Our recent survey found 22 percent of respondents **unaware** of the Main Street Lending program. And, of the respondents who want to apply for loans through the program, 81% were unable. Our survey respondents, close to this issue, suggest the removal of the following requirements, to increase eligibility and accessibility:

- Adherence to the SBA affiliate definition for various tests and restrictions (such as the employee and revenue-based tests including all affiliates, the maximum loan amount applies for all participating affiliates, EBITDA/ leverage size based tests pull in all non-participating affiliates, usage of only one type of MSLP facility for all participating affiliates, having the compensation restrictions apply to all non-participating affiliates, etc.),
- The EBIDTA/ leverage size-based test which excludes many companies early in their life cycle
- Distributions/ dividends restrictions for one year after loan payoff (especially as it applies to structuring an exit)
- Employee compensation restrictions for one year after loan payoff
- Decrease the minimum loan size

Additionally, streamline the diligence and loan underwriting process and ongoing reporting requirements and offer an asset-based loan option.

Creating greater awareness of the Main Street Lending program and increasing accessibility should result in a groundswell of applicants. The effect should help companies retain jobs and maintain operations, and consequently preserve the health care insurance for millions of Americans in this increasingly unpredictable economy tethered to the crises created by COVID-19. The Commission should recommend the Federal Reserve tailor the current program to reflect the "diverse needs" of this "broad and heterogeneous class of borrowers" and increase eligibility, especially among our lower middle market and smaller companies, and minority owned business, all of which may not have existing relationships with large commercial banks.

I appreciate the opportunity to speak on behalf of the 200,000 companies that operate in the middle market. ACG, and plenty of other business associations, are poised to support greater awareness of the program and means to increase accessibility. I'm happy to answer any questions.

Mr. HILL. Thank you, Mr. Bohn.

And now we will hear from Mr. Foster. You are recognized for 5 minutes.

Mr. FOSTER. Okay. Can you hear me.

Mr. HILL. We can.

Mr. FOSTER. Great.

STATEMENT OF VINCENT D. FOSTER, EXECUTIVE CHAIRMAN, MAIN STREET CAPITAL CORPORATION

Mr. FOSTER. Members of the Commission, thank you for inviting me today to testify on the state of the Federal Reserve's Main Street Lending Program. I am Vince Foster, executive chairman of Main Street Capital. Main Street Capital is an active member of the Small Business Investor Alliance in Washington. We provide long-term debt and equity financing to lower middle-market U.S. businesses. We currently have investments in 68 lower middle-market businesses in 26 States, in which our average ownership is 36 percent. These businesses on average each have roughly 200 employees.

The Main Street Lending Program, while enacted to assist businesses like our portfolio companies weather the economic storm brought on by the pandemic, is not responsive to their needs as currently structured. The principal structural problems are:

Number one, requiring lenders to undertake full credit underwriting for small to mid-sized borrowers seeking 3.5 percent, four to six times EBITDA loans results in a risk/reward mismatch. Lenders are better off expending their time and capital underwriting conventional loans.

Number two, requiring 15 percent amortization in year 3 of the loans is a non-market and very onerous provision, effectively requiring the loans to be refinanced after 2 years.

Number three, prohibiting contractual subordination (in the case of the new loan facility) and requiring (in the case of the priority loan facility) senior or pari passu priority to existing debt is problematic in that most companies will have preexisting senior debt outstanding, the terms of which will have to be renegotiated.

Number four, testing the maximum number of employees and revenue utilizing the affiliation rules contained in the Small Business Administration regulations applicable to 7(a) loans, without the exceptions including the PPP program, dramatically reduces the number of companies eligible for the Main Street Lending Program.

The lending facilities as currently structured are unattractive to those borrowers that are reasonably creditworthy as less restrictive financing is likely to be available from conventional sources. Yet the facilities remain unavailable due to lender reluctance to accept balance sheet exposure with respect to less creditworthy borrowers.

The following structural changes would make the program more attractive to both lenders and borrowers to advance Congress' objectives:

Number one, the loans should be unsecured and subject to preexisting contractual subordination and rank junior in priority to other preexisting senior debt.

Number two, the loans should have a term of 7 years, generally sufficient to allow them to mature after the maturity dates of pre-existing debt. Amortization should not begin until the end of year 4.

Number three, the multiples of 2019 adjusted EBITDA should be increased from 4 times in the new loan facility and 6 times in the priority facility to 6 times and 7 1/2 times, respectively. There should also be elective asset-based criteria (such as a percentage of loan-to-value and/or a 1.2 times minimum debt service coverage ratio) instead of using solely leverage multiples for all industries.

Number four, experienced nonbank lenders should be permitted to participate as eligible lenders (similar to the PPP program); the loans should have an interest rate of LIBOR plus 400 rather than 300 basis points; and the upfront origination fee payable to the lenders should be increased to 200 basis points paid by Treasury.

Number five, the affiliation rules should not limit an affiliated group to a single Main Street facility or a single lending facility's size limitation when more than one group member would like to access that or another Main Street lending facility.

And, finally number six, one of our lenders, a highly respected and conservative regional bank, has elected not to participate in the Main Street Lending Program. Instead they confirmed that their primary regulator had no issues with the bank utilizing the 1- and 2-year deferral of interest and principal feature utilized by the program in the bank's regular lending program. This will help provide certain qualified pandemic-affected borrowers the liquidity they need. Accordingly, it may be helpful to coordinate with the appropriate regulators as to whether this type of regulatory action might encourage other banks to similarly modify their lending programs to assist affected borrowers.

Thank you again for the opportunity to speak to you today, and I look forward to your questions.

[The prepared statement of Mr. Foster follows:]

Title: Congressional Oversight Commission Examination of the Main Street Lending Program

Submitted Statement of Vincent D. Foster

Executive Chairman, Main Street Capital Corporation

Before the Congressional Oversight Commission

August 7, 2020

Members of the Commission:

Thank you for inviting me today to testify on the state of the Federal Reserve's Main Street Lending Program. I'm Vince Foster, Executive Chairman of Main Street Capital. Main Street Capital is an active member of the Small Business Investor Alliance in Washington. We provide "one-stop" capital solutions for lower middle market companies seeking to grow or transition ownership. Similar to other non-bank lenders in our space, we offer entrepreneurs, business owners, management and employees a number of advantages to help each business realize its full potential.

My testimony today will focus primarily on The Main Street New Loan Facility (MSNLF) and the Main Street Priority Loan Facility (MSPLF). Main Street Capital applauds the Federal Reserve's efforts to assist our nation's small and mid-sized businesses. Our firm provides long-term debt and equity financing to lower middle market (LMM) U.S. businesses (generally those with annual revenues between $10 million and $150 million). We currently have investments in 68 LMM business in over 26 states in which our average ownership is 36%. These businesses on average each have 200 employees.

The Main Street Lending Program, while enacted to assist businesses like our portfolio companies weather the economic storm brought on by the pandemic, is not responsive to their needs as currently structured. The principal structural problems are:

1. Requiring lenders to undertake full credit underwriting for small to mid-sized borrowers seeking 3 ¼%, 4-6X EBITDA loans results in a risk/reward mismatch. Lenders are better off expending their time and capital underwriting conventional loans.

2. Requiring 15% amortization in year three of the loans is a non-market and very onerous provision, effectively requiring the loans to be refinanced after two years.

3. Prohibiting contractual subordination (in the case of MSNLF) and requiring (in the case of MSPLF) senior or pari-passu priority to other/existing indebtedness is problematic in that most companies will have preexisting senior secured debt outstanding, the terms of which will have to be renegotiated.

4. Testing the maximum number of employees and revenue utilizing the affiliation rules contained in the Small Business Administration (SBA) regulations applicable to SBA Business Loans (e.g., 7(a) loans) dramatically reduces the number of companies eligible for the Main Street Lending Program. For example, if a business with 250 employees is owned by an entrepreneur who controls another company in an unrelated industry that also employs 300 employees, then both businesses are considered to employ over 500 employees, and neither business is eligible for an SBA Business Loan. This same concept is used for determining Main Street facility eligibility. Once affiliation has been

established, the affiliated group of companies (with limited exceptions) must share a single Main Street facility limitation amount (e.g., the lesser of 4X the company's 2019 adjusted EBITDA or $35 million for MSNLF loans, minus the amount of pre-existing indebtedness). As larger private companies are more likely to have sister companies that are under common control with them, this non-statutory test substantially reduces the number of these companies eligible for Main Street loans. Under the PPP program, commonly-controlled business entities are able to at least share double the single-company loan limitation of $10 million. The PPP loans were largely designed to be grants to less than 500 employee businesses; the Main Street loans in contrast must be fully repaid and can be extended to up to 15,000 employee companies, or groups of companies. Why should two companies under common control that each employ a total of 200 employees and have $20 million of preexisting debt be able to access up to $20 million in potentially forgivable PPP loans, while two companies each employing 7,000 employees and with preexisting debt of $20 million can only access $15 million (e.g., $7.5 million each) of MSNLF loans that must be repaid?

The lending facilities as currently structured are unattractive to those borrowers that are reasonably creditworthy as less restrictive financing is likely to be available from conventional sources. Yet the facilities remain unavailable due to lender reluctance to accept balance sheet exposure with respect to less creditworthy borrowers. So while the facilities may be acting as a "backstop" to currently available financing options in case economic conditions deteriorate, they are not advancing the policy goals of assisting those companies that either did not qualify for PPP loans (e.g., they had greater than 500 employees on their payroll or by attribution), or did qualify and receive PPP assistance, but are in need of a longer term financing solution in order to maintain their current payroll levels.

The CARES Act as enacted by Congress grants the Federal Reserve and Treasury adequate flexibility to provide financial assistance to companies having fewer than 15,000 employees or less than $5 billion in annual revenues. However, the rules developed by the Federal Reserve to implement the program are too restrictive and burdensome to address the current need. Understandably, these rules operate to protect the government against credit losses, but credit losses will have to be incurred in all likelihood if these companies are going to receive the financial assistance Congress intended. Secretary Mnuchin acknowledged this reality when he stated that the Treasury Department was "fully prepared" to incur losses on the CARES Act facilities. The following structural changes would make the program more attractive to both lenders and borrowers to advance Congress's objectives:

1. The loans should be unsecured and subject to preexisting contractual subordination and rank junior in priority to other pre-existing senior indebtedness.

2. The loans should have a term of 7 years, generally sufficient to allow them to mature after the maturity dates of pre-existing indebtedness. Amortization should not begin until the end of year 4.

3. The multiples of 2019 adjusted EBITDA should be increased from 4X (MSNLF) and 6X (MSPLF) to 6X and 7.5X, respectively. There should also be elective asset-based criteria

(such as a percentage of loan to value and/or a 1.2X minimum debt service coverage ratio based on 2019 adjusted operating income) in lieu of using solely leverage multiples for all industries.

4. Experienced non-bank lenders should be permitted to participate as Eligible Lenders (similar to the PPP program); the loans should have an interest rate of LIBOR plus 400 rather than 300 basis points; and the upfront origination fee payable to the lenders should be increased to 200 basis points and be paid by Treasury (similar to the PPP program).

5. The affiliation rules should not limit an affiliated group to a single Main Street facility or a single facility's loan limitation if the group as a whole generates less than $5 billion in revenue and employs fewer than 15,000 employees, and more than one group member would like to access that or another Main Street facility.

6. One of our lenders, a highly respected and conservative regional bank, has elected not to participate in the Main Street Lending Program. They instead confirmed that their primary regulator had no issues with the bank utilizing the 2-year deferral of interest and principal feature utilized in the MSNLF and MSPLF in the bank's regular lending program to help provide certain qualified COVID-affected borrowers the extra liquidity they need to navigate the pandemic. Accordingly, it may be helpful to coordinate with the appropriate regulators as to whether this type of regulatory action might encourage other banks to similarly modify their lending programs to assist affected borrowers.

Respectfully Submitted,

Mr. HILL. Thank you, Mr. Foster.

And now, Ms. Mills, you are recognized for 5 minutes.

STATEMENT OF GWEN MILLS, SECRETARY TREASURER, UNITE HERE

Ms. MILLS. Thank you, members of the Commission. My name is Gwen Mills. I am secretary-treasurer of the hospitality union UNITE HERE. While I will focus on our members' experiences, the recommendations I make are supported by the AFL–CIO, representing 55 national unions and 12 million workers.

Our 300,000 members work primarily in the hotel, casino, food service, and airline catering industries—all sectors that are heavily dependent upon travel and tourism.

Before the CARES Act became law, 90 percent of our members were laid off. Today 85 percent remain unemployed.

A majority of our members are women and people of color. Many are recent immigrants. Most have lost or will soon lose their health care—benefits won often after giving up wage increases to secure family health care.

Hundreds of our members or their family members have died from coronavirus—22 in Las Vegas alone, where 350 have been hospitalized.

Our industries are the most severely affected in terms of unemployment, so I believe our story is a cautionary tale of what awaits American workers across the board if we fail to correct course.

At heart is the question of requiring employers to maintain employment as a condition of Federal assistance. The Main Street Lending Program requires only commercially reasonable efforts to maintain employees in spite of clear congressional intent. Treasury and the Federal Reserve said they will not enforce even that.

We have seen this movie before, and we know how it ends for working people. We have seen how powerful lobbyists transform the PPP and Payroll Support Programs into subsidies for real estate investors.

We have identified 200 outlets where we have members that received PPP loans, and they have not protected paychecks or health care.

One company—Omni Hotels—received 34 PPP loans worth at least $53 million. Meanwhile, Omni hotels in Boston, Providence, and New Haven were shut down in March, and it is unclear when they will reopen. In Providence, the company then cut off medical benefits in violation of their union agreement, and there are many similar stories.

What they reveal is how a powerful industry turned a program designed to keep workers on payroll into one that could keep hotel owners current on their mortgages.

The Main Street Program will yield even worse results for workers if this mission drift is allowed. Now hotels demand a bailout of $86 billion worth of CMBS loans using the Main Street Program. This Commission reported that the Fed has considered establishing an asset-based lending facility that we fear would do just that.

Who would benefit most from a hotel CMBS bailout? Lobbyists want you to believe it would mom-and-pop hotels. But the largest beneficiaries are sophisticated real estate investors.

Our analysis of loan data finds that: the 11 largest borrowers had at least $1 billion each in hotel CMBS; those 11 had a combined $30 billion in loan balances or about a third of the total outstanding; four were private equity firms, two were REITs, one a hedge fund billionaire, and the rest were developers or billionaire investors. The 12 belong to the Fontainebleau Miami Beach, whose owner refinanced its debt twice in 2 years, borrowing more to cash out millions. Now Fontainebleau has stopped health care for hundreds of laid-off employees despite subsidies provided by the Employee Retention Tax Credit.

Lobbyists claim if the Fed does not rescue CMBS borrowers, hotels will default and workers will not have jobs to come back to. But that is not our experience, and this is not the first time hotel owners got themselves in trouble using these inflexible loans. After the financial crisis, there were scores of defaults across the country. But defaults and foreclosures did not lead to closed hotels. Hotel workers who are used to seeing absentee owners come and go understand that jobs are driven by occupancy, and only ending the pandemic can fix that.

Almost half of hotel CMBS mortgages mature within 2 years, before the industry is projected to recover. Should the Fed refinance the entire hotel lending market while real estate investors lay off 85 percent of hotel workers and end their health care in a pandemic?

There is a second critical lesson here which relates to the Main Street Program. There is no question that stabilizing credit markets is extremely important in a crisis, and the Fed has done that. But the real mission should be to protect jobs of American workers. The exclusive focus on markets and not on jobs means our members, most of whom are brown and black, are thrown off payrolls while their employers, whose boards and shareholders are predominantly white, can simply tap their credit lines and ride out the crisis.

It is no longer acceptable for the Fed to just stand by and watch us fall off a fiscal cliff. Millions of American workers are right behind us on the precipice.

Instead, what if program designers at the Fed take the CARES Act mandate to heart? What if credit terms were loosened so long as—and here is the important part—so long as there were airtight requirements, not incentives, not recommendations, but requirements that recipients keep workers on payroll? It is what the PPP could have done if it had not been hijacked by the real estate industry.

The Fed and Treasury must learn from PPP and reform Main Street lending so that it actually contributes to the employment of working Americans. But please do not bail our real estate investors while they push workers off the cliff.

Thank you for this opportunity, and I welcome your questions.

[The prepared statement of Ms. Mills follows:]

TESTIMONY OF

GWEN MILLS

BEFORE THE

CONGRESSIONAL OVERSIGHT COMMISSION

AUGUST 7, 2020

Members of the Commission, my name is Gwen Mills. I'm Secretary-Treasurer of UNITE HERE, the North American hospitality union. I appreciate this opportunity to address the Commission today. While my testimony will focus on our industry and the experience of our members, the policy recommendations I will make have the support of the AFL-CIO, representing 55 national unions and 12 million workers.

Our 300,000 members throughout the US and Canada work primarily in the hotel, casino, institutional food service, airline catering and airport retail industries – all sectors that are heavily dependent upon the travel and tourism economy.

Our members have been among the most severely affected by the pandemic. Before the CARES Act became law, 90% of our members had been furloughed or laid off. Today little has changed: about 85% of our members remain unemployed.

A majority of our members are women and people of color. Many are recent immigrants. Most of them have lost or will soon lose their health insurance – benefits that they only won after decades of hard-bargained contracts, often giving up wage increases in order to maintain good family healthcare.

Hundreds of our members or their family members have died from coronavirus – 22 in Las Vegas alone, where an additional 350 have been hospitalized.

A Cautionary Tale

The industries in which our members work have been the most severely affected in terms of unemployment, so I believe our story is a cautionary tale of what awaits American workers across the board if we fail to correct course.

At the heart of this is the question of requiring employers to maintain employment as a condition of federal assistance. There is no requirement in the Main Street Lending Program in spite of clear Congressional intent. This is because the Federal Reserve and Treasury, as part of their April 30 revisions to the facility term sheets for the Main Street Lending Program, eliminated the requirement that loan applicants make "reasonable efforts" to maintain payroll and retain employees during the term of their loan. Under the revised term sheet, firms need only make "commercially reasonable efforts" to maintain payroll. Not only does that make lawmakers' vague mandate even vaguer, but Treasury subsequently clarified that it had no intention of enforcing even that weakened standard. Apparently making "commercially reasonable efforts" is non-binding advice.

We've seen this movie before. And we know how it ends for working people. Because we have seen what happened in other CARES Act programs.

We've seen how powerful hospitality and real estate industry lobbyists with access to the halls of power have been able to transform CARES Act programs like the Paycheck Protection Program and the Payroll Support Program, which were designed to keep furloughed workers connected to their jobs by keeping them on payrolls with continuation of benefits, into subsidies for real estate investors.

We've identified more than 200 hotels or food service outlets where we have members that received PPP loans, according to data recently released by the SBA. I've provided a few case studies in the appendix, but suffice it say the program hasn't protected paychecks or healthcare for the vast majority of our members, 85% of whom remain unemployed more than four months after passage of the CARES Act.

One company - Omni Hotels, received at least thirty-four separate PPP loans with a combined value between $53 million and $123 million, according to the SBA data.[1] Meanwhile, Omni hotels in Boston, Providence, and New Haven were shut down in March and our members laid

[1] It is possible that some of the loans Omni affiliates received were returned, since it is our understanding that not all returned PPP funds were reflected in the data released by the SBA.

off, and it is unclear when the properties will reopen. In Providence the company cut off medical benefits at the end of May, which we believe is in violation of their collective bargaining agreement. In several other cities where workers get health insurance through a jointly-administered Taft-Hartley health fund, the company is no longer paying medical insurance premiums for their laid-off workers.

There are many similar stories I could tell. And I've included a few others in Appendix A.

What they reveal is how a powerful industry lobby largely succeeded in transforming a program designed to stabilize small businesses and help keep workers on payroll into a program that could keep hotel owners current on their mortgages for a few more weeks.

Given this mission drift with respect to a program that lawmakers clearly intended to support payrolls, we have every reason to believe the Main Street program will yield even worse results for workers. First, we're unaware of a single one of our employers that has sought or received a Main Street loan. And even if one did, the Treasury and Fed have been crystal clear that they have no intention of ensuring that the loan proceeds will be used to keep workers on payroll.

Now hotel industry lobbyists have joined forces with lobbyists representing shopping malls and other commercial real estate investors to demand a bailout of the commercial mortgage-backed securities (CMBS) market, especially the $86 billion in CMBS hotel loans. And the vehicle with which it hopes to accomplish this goal is the Main Street Lending Program.

And that's why we were alarmed to read in this Commission's third report that according to Secretary Mnuchin, the Federal Reserve has considered establishing an asset-based lending facility, which we fear would be a major step towards the hotel and shopping center CMBS bailout the real estate industry seeks.

Who would most benefit from a hotel CMBS bailout? Its proponents would have you believe it would primarily be mom and pop small businesses. But the largest beneficiaries would most likely be publicly-traded real estate investment trusts (REITs) like Monty Bennett's Ashford companies and giant private equity firms like Tom Barrack's Colony Capital.

We recently reviewed CMBS hotel loan information from data service Trepp and found that:

- There were 11 borrowers whose affiliates had at least a billion dollars in outstanding hotel CMBS balances.
- Those 11 borrowers had a combined $29.9 billion in outstanding loan balances or about a third of the total amount of outstanding hotel CMBS debt.
- Four of them were private equity firms, two were publicly-traded REITs, one was a hedge fund billionaire, and the remaining four were real estate developers or billionaire investors.
- And the 12th belongs to the Fontainebleau Miami Beach resort, which refinanced its mortgage twice in two years, borrowing more each time for the owner to cash out $191 million late last year. Now in the crisis, Fontainebleau has canceled healthcare for hundreds of laid off employees despite the subsidies provided by the CARES Act's Employee Retention Tax Credit.

These are hardly the small business owners the proponents of this bailout claim to champion.

Hotel lobbyists claim if the Fed doesn't open up the MSLP to CMBS borrowers, hotels will default and shut down, and workers won't have jobs to come back to. But that is a completely spurious contention, one not borne out by recent experience. This isn't the first time we've seen REITs and large hotel corporations get themselves in trouble using low-cost but inflexible CMBS loans. In the years following the financial crisis, there were scores of defaults across the country.

In many cases borrowers – including some of the same ones currently clamoring for a bailout– walked away from their properties and handed over the keys to lenders. But defaults and even foreclosures did not lead to hotels being shut down. new investors emerged to take ownership and kept properties running. Owners don't generally employ hotel workers anyway. They hire operating companies like Marriott, Hilton or Hyatt under long-term management agreements that frequently outlive multiple changes in ownership. Hotel workers are used to seeing absentee owners come and go. They understand that defaults, distress sales and even foreclosures don't generally affect employment levels. What affects employment levels is hotel occupancy and revenue, which is to say the level of demand for hotel rooms. Only ending the pandemic, and/or the widespread availability of effective testing and treatments, can start to fix that. Meanwhile, the Main Street program is doing nothing for hospitality-industry workers, or any workers as far as we can tell.

Just as a CMBS bailout would have little to no effect on hotel employment, we doubt it would offer much relief to the thousands of small business hotel owners whose cause the bailout proponents purport to champion, most of whom have regular bank loans.

In fact, it could hasten their demise and here's why: many of the primary beneficiaries of a CMBS bailout would be the very same private equity firms and investors who could end up in the best position to buy up the highly-discounted or foreclosed non-CMBS hotels from desperate owners whose 90-day bank forbearances have expired and whose PPP proceeds have been spent.

Not only would a CMBS bailout allow billionaire and private equity owners to escape the consequences of their own risk-taking, it would enable the largest hotel owners to acquire distressed assets with their store of "dry powder" instead of committing some of those funds to saving their own hotels.

Moreover, once the Fed starts bailing out CMBS borrowers in the hotel industry, it will not be able to stop. The debt crisis in hotels is not a short-term problem. Hotels are asking for 2 years' worth of interest payments on CMBS debt, but what they aren't telling the Fed is that $40 billion of hotel CMBS mortgages mature by 2022. In order to refinance those mortgages and repay Fed loans or "preferred equity", hotel asset values need to reach pre-COVID levels to borrow at customary loan to value ratios. Hotel asset values will lag recovery of revenues which analysts aren't projecting to happen until late 2023. How will the Fed recoup its investment in hotels if the underlying mortgages default at maturity in the coming years, or is the Fed really being asked to refinance the entire hotel lending market? The very leverage levels that prevent hotels from accessing the Main Street Lending Program portend defaults to come even after Fed assistance.

Isn't there a moral hazard in making taxpayers party to the financial engineering which has brought us to this brink, where real estate investors lay off 85% of hotel workers, end their healthcare in a pandemic and use federal assistance to pay their banks and bondholders?
In this respect, the bifurcated world of hotel asset owners is no different than the divide between small and large firms in the larger economy, which is to say large corporations have access to the credit markets but their smaller competitors, many of them family-owned businesses, usually do not.

There is a second critical lesson here for the Commission in relation to the Main Street Lending Program. There is no question that stabilizing public and interbank credit markets is extremely important in a crisis. But when the Fed acts as if its only mission or authority in times of crisis is to stabilize credit markets - whether that means bond markets, repo markets, or asset-based markets - it is making a choice. It means we should expect wildly disparate and unequal outcomes. The real core mission in this crisis should be to protect jobs and incomes of America's working people. And in the case of the CARES Act, the Congress explicitly authorized the Treasury to capitalize programs like the Main Street Lending Program so that the Fed can take credit risk in for the purpose of protecting jobs.

But the focus on the solvency of pyramided credit structures rather than on jobs means the benefits of stabilizing those credit markets are tenuous at best for workers.

It means our members – most of whom are brown and black - are thrown off payrolls and into unemployment while their large employers – whose executives, boards and shareholders are predominantly white -- can simply tap their credit lines, stockpile cash and ride out the crisis.

The Federal Reserve is now trying to implement the Main Street Lending Program at a moment when the fate of 30 million unemployed and their families is in the hands of a deadlocked and dysfunctional Congress, where despite the fact that the HEROES Act is sitting on Leader McConnell's desk, our members are exposed to the full consequences of time-limiting the pandemic unemployment benefits and then letting them expire for our families lives and health.

It is no longer acceptable for the Fed to just stand by and watch us fall off that cliff. Read the room. Millions of American workers are right behind us and on the precipice.

In this context, the choice to leave the MSLP dying on the vine seems at best unimaginative, and at worst destructive. One can certainly argue, as Chairman Powell has, that the reticence of banks to make the loans and the putative lack of interest by prospective borrowers are signs that private markets are working and there is no urgent need for the program at the moment.

But what if lawmakers had been clearer in their proscription that the program help businesses stay connected to their workforces? What if the program designers at the Fed had taken that mandate to heart? What if credit terms were loosened considerably what if we actually used the Treasury capital as Congress had intended – up to and including making loans forgivable in some circumstances – so long as – and here's the important part – so long as there were air-tight requirements – not incentives, not suggestions, not recommendations – but requirements that recipients keep workers on payroll?

Short of making direct grants to workers to substitute their lost income and healthcare – something presumably only Congress can do – tying credit assistance to payroll in a reinvigorated MSLP is the one new thing the Fed could do right now to really make a difference in the lives of millions of American workers and their families.

It is what the PPP could have done if it hadn't been hijacked by the real estate industry.
The Fed and Treasury must learn from the PPP experience. The Fed and Treasury must reform the MSLP so that it actually contributes to the economic security and employment situation of working Americans.

That, in our opinion, would be the best thing the Fed could do with its mostly-unused MSLP authority to help average Americans. And we've already said what we think would be the worst.

Thank you on behalf of the working people I represent for the chance to appear before this Commission's first hearing. It means a lot to us. And I welcome your questions.

Appendix A: Case Studies

<u>OTG</u>

OTG is one of the largest operators of airport restaurants in the United States, with significant presence at key hubs in New York / New Jersey, Philadelphia, Houston, Minneapolis and Washington, DC. According to the SBA data, the company was approved for 8 separate PPP loans totaling between $18 million and $50 million. In March, the company was featured in the *New York Times* for abruptly laying off 1,200 workers at the New York-area airports and cutting those workers off their health insurance effective March 31st.[2] Most of those workers remain unemployed and the company to our knowledge has not extended health insurance to those workers who were laid off.

Payroll Support Program – Where's the Support for Airline Catering Workers?

When lawmakers created the Payroll Support Program for the aviation industry, they included airline catering contractors. That should have meant continued paychecks for thousands of airline catering workers from April through September and no layoffs. Yet, Gate Gourmet, which received $171 million from the program, laid off approximately 5,000 of its 8,000 U.S. employees in May and hasn't recalled them. Another contractor, Flying Food, received $85 million and also laid off thousands of people. At the company's kitchen serving Dulles Airport, only 2 out of 168 workers were working in June, after the company reached its agreement to receive millions in taxpayer funds from the payroll support program.

How did this happen? First, the Treasury issued guidance explicitly allowing employers to spend funds indefinitely, rather than imposing a deadline for companies to use the funds. A deadline would ensure workers promptly received money intended for them. Second, the Treasury took months to implement the agreements that could have prevented layoffs had they been executed

[2] https://www.nytimes.com/2020/03/21/nyregion/coronavirus-airport-workers-ny-nj.html

quickly. These firms were allowed to lay off thousands in April and May, take federal funding in June and July, and hold those funds indefinitely to subsidize their future payroll whenever they decide to start bringing back workers. In the meantime, they are not required to do anything to assist their laid off workers. Like the PPP, a program meant to protect paychecks became one that instead protects corporate bottom lines.

Appendix B: The Hijacking of the PPP

An early prototype of what became the PPP was a plan floated in mid-March by the hotel lobbying group American Hotel and Lodging Association. Their proposal, which they called the "Hospitality Workforce Relief Fund"[3] called on Congress to provide $100 billion in "grants to businesses for the purpose of employee retention and rehiring" and an additional $50 billion "to provide federal funds to cover debt payments" for hotel owners and "to facilitate forbearance" on the part of hotel lenders. Around that same time, the head of the AHLA and the leading hotel industry CEOs met in closed door session with President Trump and Vice President Pence to promote their plan.[4]

AHLA subsequently took credit for winning an unusual carve-out for their industry in the plan that emerged in the final package of the CARES Act. That provision singled out hospitality companies – those with NAICS codes beginning with 72 – for special treatment, exempting them from the SBA's affiliation rules, thus making it possible for large hotel and restaurant corporations to apply for and receive PPP loans at every one of their locations with fewer than 500 employees. That is how companies like Omni were able to receive so many PPP loans.

Despite this unprecedented carve-out, AHLA was not satisfied. Beginning the day after the CARES Act became law, the group criticized the new program, calling it "unworkable for hoteliers" because, they argued, its focus on payroll expenses was too restrictive and would not enable hotel owners to cover their monthly mortgage payments, particularly those hotel owners locked-in to an inflexible kind of loan known as a commercial-mortgage backed security (or CMBS) loan.

[3] https://www.ahla.com/sites/default/files/HospitalityWorkforceReliefProposal.pdf
[4] https://thehill.com/business-a-lobbying/business-a-lobbying/488084-tourism-industry-calls-for-150-billion-in-assistance

Industry efforts to shoehorn the program into a mortgage subsidy culminated in the PPP Flexibility Act, which went a long way toward transforming a program designed to stabilize small businesses and help keep workers on payroll into a program that is more likely to keep hotel owners current on their mortgages for a few more weeks.

Supplemental Points for the Record, CARES Act Oversight Commission Hearing, 8/7/20, Submitted by Gwen Mills, Secretary-Treasurer of UNITE HERE

The following facts elaborate on the summary of large CMBS borrowers provided in my testimony and respond to the comments made by Commissioner Hill at the hearing that 74% of CMBS are less than $20 million and owed by small businesses. We believe hospitality CMBS loans differ from that profile significantly.

We analyzed hospitality CMBS loan data from Trepp, a data service tracking CMBS loans. Our analysis finds that:

- 59% of hotel CMBS loans had outstanding balances of $20 million or more, and 76% were over $10 million.
- Of the $86 billion outstanding in lodging CMBS loans, at least $50 billion (58%) are affiliated with large, multi-property hotel owners, private equity firms, hedge funds, REITs, or foreign capital.
- The largest 11 borrowers had at least $1 billion each in hotel CMBS, and together they had $30 billion in loan balances or about a third of the $86 billion outstanding in the industry.
- Four of the top 11 borrowers were private equity firms, two REITs, one a hedge fund billionaire, and the rest were developers or billionaire investors.

Based on this data, the hotel industry's asset-backed loans are dominated by large, sophisticated real estate investors, many with access to an array of capital sources.

This analysis leads us to ask what the goal of an asset-based lending facility backed by the Federal Reserve should be. We firmly believe that the goal of any Federal Reserve rescue plan, including an asset-based facility, should be to maintain payroll, benefits and recall rights for workers. If the goal of an asset-based lending facility is narrowly construed as keeping owners out of default, that is not a policy goal worth spending taxpayer resources on.

We urge the Federal Reserve to mandate that any relief from an asset-based facility be conditioned on maintaining pre-COVID payroll and benefits for hospitality workers; prohibit the use of proceeds to fund distributions or dividends on equity, related-party transactions, and franchise fees; and cap proceeds of the facility to affiliated companies in order to ensure the relief is not concentrated in large hotel and real estate owners.

Mr. HILL. Thank you, Ms. Mills. Appreciate your testimony today.

We will now have a round of questioning, and I recognize myself for 5 minutes.

Let us start with Ms. Anderson. You were talking about your view of the banks taking up of these loans and what modifications might be made for less than creditworthy borrowers. I understood that point. But as I said in my earlier questioning, 5,000 banks jumped on the opportunity to help in the PPP environment under the CARES Act, and we have got very few banks that are engaging here.

What is the Bank Policy Institute doing to promote banks participating in the Main Street Program?

Ms. ANDERSON. Thank you for your question. In terms of BPI member banks, the vast majority of our members are participating in the program. I cannot speak, obviously, for all banks across the country, but I think when you think about the complexity of the program, it is difficult not just for small borrowers but also for smaller lenders. The program is set up as a participation structure, which is typically used in the syndicated loan market. Many smaller banks may not actually be active in that space, familiar with it, and there is quite a lot in terms of going through the legal documentation and setting up the infrastructure to actually lend in that manner and comply with the terms of the program. So while we certainly have our members participating, it may be more challenging for smaller banks.

Mr. HILL. Thank you. And do you agree with the testimony on our panel that it is possible to make a very creditworthy loan that is not based on the EBITDA multiples and the senior nature of the term sheet? In other words, that if one were to have sufficient collateral coverage and a 1.25 debt service coverage ratio but a junior lien, wouldn't that be considered a creditworthy loan as well?

Ms. ANDERSON. So a number of our members have said that they would be interested possibly in lending at a junior facility, something that is collateralized. I think it would be up to the Fed and the Treasury to decide exactly what their risk appetite would be in such a structure and structure the terms appropriately. So it may not be 1.2 but something similar. So, yes, I do think banks would be interested if there was a junior facility available.

Mr. HILL. Do you think the Fed and the Treasury are not setting the risk parameters appropriately in their existing Main Street term sheets? In other words, are they too strict? Are they too much like a traditional senior bank loan with not even a step in the direction towards a slightly distressed—solvent, creditworthy, but distressed, temporarily distressed borrower?

Ms. ANDERSON. So I think the eligibility criteria that the Fed and the Treasury established probably fit the program that they set out to design, as President Rosengren said, in terms of the liquidity program. But there is a key element. So even if you reduced some of the stringency of those terms, you still have the underwriting element. And in this environment, underwriting on today's information will be difficult for many borrowers in that distressed space. So I am not sure that actually loosening the criteria is necessarily the right answer.

But I think also in terms of what President Rosengren said, if companies really need equity, then a Federal Reserve lending program is not the right solution for them.

Mr. HILL. Understood. Thank you for your response.

Mr. Bohn, let us talk about the affiliation rules. You heard my conversation with Dr. Rosengren that the Fed here in the Main Street Facility has adopted those Small Business Administration 7(a) lending affiliation limitations. For this middle market of non-super small businesses and certainly those not eligible to raise capital in the public markets, are those affiliation rules a serious impediment? And can you give us an example?

Mr. BOHN. Thank you, Congressman. I think that what we are seeing and hearing and what was evident in the survey that we had is that these businesses were originally excluded from the PPP, and there was hope initially that in the Main Street lending provision that there would be opportunities for them to utilize benefits and lending from Main Street in order to not only keep jobs but also invest in some of the changes that they need to do as people start to pivot based on the economy and whether that is setting up plexiglass and rearranging their buildings or whether or not that is related to simply doing business in a much different way. But we have heard from them loud and clear that their inability to access them has had a significant impact on their business. When we first went out there and talked to our members——

Mr. HILL. Thank you. Let me—thank you for that. We will have another round, but my time has expired.

Let me turn to Mr. Ramamurti for 5 minutes.

Mr. RAMAMURTI. Thank you, Mr. Chairman. And thank you, Ms. Mills, for your testimony today. You noted in your written testimony that hundreds of your union's members and family members have died from COVID, and many more have been hospitalized. I just want to extend my condolences to them and their families and to you, and I think it is a powerful reminder that this is first and foremost a health crisis, and that front-line workers like the people that you represent are bearing the brunt of it.

You represent a lot of people who work in hospitality and in tourism as front-line service workers, hotel housekeeping, bellmen, wait staff, cooks, bartenders, casino workers. You mentioned in your opening statement that a majority of your members are people of color and that a majority are women.

When the companies who employ your members struggle, who are the first people to suffer via layoffs or furloughs?

Ms. MILLS. Yeah, thank you for your question. Across the board it is the front-line workers first, our members, who are laid off.

Mr. RAMAMURTI. Right.

Ms. MILLS. And our experience is that the white middle management are able to keep their jobs.

Mr. RAMAMURTI. And when they are laid off or furloughed, it is not just lost income, right? In many cases they are losing access to health care, to retirement contributions, and to other benefits?

Ms. MILLS. Absolutely, yes.

Mr. RAMAMURTI. And so among the hundreds of thousands of travel and tourism industry workers that you represent, 4 months into this crisis are you aware of a single job that has been saved by the Main Street Program or even a single hours cut or furlough that the Main Street Program has stopped?

Ms. MILLS. No.

Mr. RAMAMURTI. And as the Main Street Program is currently designed, do you think it will help workers in the future, even if more companies participate in it?

Ms. MILLS. No. As I said in my testimony, not without binding requirements that employees be rehired from the first day of the aid.

Mr. RAMAMURTI. Right. So, in other words, even if a lot of companies end up getting loans through this program, you do not think that the benefits of those loans will flow through to workers?

Ms. MILLS. No, not without binding requirements.

Mr. RAMAMURTI. So 45 million people work at companies that are eligible for the Main Street Program. If the goal is to help those millions of workers, do you think the Fed can just make tweaks to the Main Street Program to achieve that? Or do you think Congress needs to come up with a brand-new approach?

Ms. MILLS. In this case I do not think tweaks will work. I think Congress does need to come up with a new approach.

Mr. RAMAMURTI. So let us talk about that a little bit. In your experience, what kind of new approach do you think would be helpful to your workers? In your experience and the experience of your members, does providing financial support to businesses help workers without express and enforceable requirements that businesses actually use that aid to support workers?

Ms. MILLS. No. Time and again in many different programs, without enforceable requirements, support to businesses does not help workers.

Mr. RAMAMURTI. So of the $500 billion that Congress gave to the Treasury in the CARES Act in March, there is currently more than $200 billion sitting unused and uncommitted. If you were to use that money to develop a program that would be most helpful to your members, what would you do with it?

Ms. MILLS. The two things that matter are health care and wages, so we would fund COBRA payments so that we could continue health care, and then give direct support to workers.

Mr. RAMAMURTI. Thank you. And one final question about this. Did the Treasury Department ever reach out to your union as it was designing this lending program that was ostensibly about helping workers?

Ms. MILLS. No.

Mr. RAMAMURTI. Thank you, Ms. Mills. Look, I share your views and, frankly, I think it is time we started to listen to working people, not executives and investors and their lobbyists, when we design these programs that are supposed to be ultimately about helping workers.

Thank you, Mr. Chairman. I yield back.

Ms. MILLS. Thank you.

Mr. HILL. Thank you, Mr. Ramamurti.

Congresswoman Shalala is recognized for 5 minutes.

Ms. SHALALA. Thank you. Let me follow up with Ms. Mills since I represent a district that has a huge number of workers that work in the tourism industry, particularly in the hotels, including the Fontainebleau, which you mentioned.

We had a debate with the Fed over whether their term "commercially reasonable" was better than "reasonable," but it sounds to me from what you said that either one does not mandate that these programs keep people employed or even furloughed workers keeping their health care so that they can get on unemployment and keep their health care. I take it that we would have to really fine-tune that requirement in these programs to make a difference for not only the workers that UNITE represents, but the thousands of workers that work in this industry.

Ms. MILLS. Yes, thank you, Congresswoman, for your question. I mean, our great concern about the Main Street Lending Program is that the hotel industry is seeking changes so that they can use the program to pay their CMBS mortgages, like there is a $975 million loan at the Fontainebleau Miami Beach that is in your district. As I mentioned, the Fontainebleau stopped paying health care for hundreds of our laid-off members. We believe it is a violation of our contract, and so it would be wrong for taxpayers to fund a year or two worth of Fontainebleau's debt payments of $39 million a year while laid-off workers lose their health insurance and rely on the public hospital system. So fine-tuning absolutely requirements would be necessary, and I really appreciate your question today because one of the Fontainebleau workers died this morning of COVID in the hospital without his medical or life insurance.

Ms. SHALALA. I heard that, and I am so sorry. I want to point out that those workers are also taxpayers, because we are talking about their money being used for the mortgage payments.

So you do not see anything in the Main Street Program that could be significantly improved unless it was totally restructured in terms of helping workers in this country?

Ms. MILLS. I think that is right. It would need to be restructured with requirements off the bat for bringing workers back as soon as any assistance was issued, yes.

Ms. SHALALA. Well, thank you very much.

Let me ask Ms. Anderson a question. The Main Street Lending Program allows banks to employ their own underwriting standards to loan applications. Does that mean that banks are making loans under the program that they would have made anyway absent the Fed program? And if so, is the Main Street Lending Program providing any benefit to borrowers at all?

Ms. ANDERSON. Thank you for your question. In terms of the loans that are being made, I think they are quite specific in terms of the circumstances, because you are absolutely right, a borrower who can meet a bank's basic underwriting standards is typically finding out that there is a product that is more suited to them given their credit needs. So, for example, maybe a term loan really is not what they need and they really need something more like a flexible working capital facility. So our banks are actually many times finding better solutions for these borrowers when they inquire about the program.

In terms of the live cases that look like they might go through, one example is a travel company that basically came to one of our banks as a new lender—a new borrower, sorry, and the bank would be comfortable possibly lending the 5 percent. And in a normal circumstance they would go out and syndicate that loan to the market. But given the timing that it takes to do that and the need to actually get finances to these borrowers, that is one where they think it makes sense to use Main Street because the Government is there ready and waiting, so they do not have to go through a syndication process. But, you know, whether there are lots of borrowers in those specific circumstances I think is questionable.

Ms. SHALALA. One more quick question. Many of the small to mid-sized businesses that were able to get by in the first few months, they used the PPP program, are now at the end of their ropes. Goldman Sachs reported that more than 80 percent will be out of PPP money. If that is the case, where are they turning for funding? Are your banks seeing an uptick in loan requests?

Ms. ANDERSON. I would not say we are seeing a huge uptick in loan requests, but something that is interesting is that the vast majority, so probably over 70 percent, of new borrower inquiries that our banks are getting are actually borrowers who think Main Street is a PPP program. So they think it is a loan forgiveness program or a grant program. And once they hear the details, then they realize it is actually not for them. So they are looking for something that is equivalent to a PPP type structure.

Mr. HILL. Thank you.

Ms. SHALALA. I yield back.

Mr. HILL. Yes, thank you, Congresswoman Shalala. Your time has expired.

Now we will turn to Senator Toomey for 5 minutes.

Senator TOOMEY. Thank you, Mr. Chairman.

I just want to go back and review very briefly a little bit of the history about how these programs came together, because we debated the extent to which we should have mandates to retain a workforce and how best to do that. And for small businesses, we thought that it might be possible for businesses, even businesses that are essentially closed, have no business, it might be possible to maintain the payroll if we pay for it, if we had the taxpayers pay for it. And so that is what the PPP program was designed to do, take a finite period of time and have the taxpayer just pick up the tab for the payroll. And to a very significant degree, I think it has worked, and it was probably necessary.

With the Main Street Lending Program, the idea was that these would be loans. And while obviously everybody wants to maximize employment opportunities, maximize jobs, we are all celebrating record-low unemployment, record-high job opportunities for everybody in America, most especially the African American community, the Hispanic community, people who have historically have higher rates of unemployment. We are seeing tremendous gains. This was all great.

But the idea that we would require companies to borrow money for the purpose of maintaining a payroll for people who they did not have work for because the business was closed, that did not seem to make sense, which is why we made unemployment benefits more generous; we did direct payments of $1,200 to everyone to offset the lost income that was notable.

So let me try to illustrate this another way with a question, and maybe Mr. Bohn or Mr. Foster would want to take a shot at this. If a business is losing money, probably massively, as it collapses in sales, has no orders coming in because of this contraction that was underway, and hopefully is in the process of getting behind us, and, therefore, has no work for its workers, if that business goes out and borrows a lot of money to pay those workers anyway, does that make that business more viable, more likely to succeed, more likely to be there at the end of this contraction to be able to bring workers back?

Mr. BOHN. Well, Senator Toomey, thank you. If I could, I will take a stab at that. I think what we are talking about here is really two separate things. I think, yes, PPP was definitely designed to save jobs in the immediate term and as quickly as possible. What we are hearing and seeing from middle-market organizations, though, is that the loans, if they were able to get them, would go to investment in opportunities that would create jobs or bring back jobs within their company. So if you even use the example of ACG as an organization, there is a lot we have to do and do not have the finances to be able to really exist well equipped in this new virtual environment. We are seeing that time and time again, whether it is for our restaurants and how they are having to handle how they prepare for orders and utilize technology, so there are opportunities. But at the end of the day, it is a moot point because there is such a large number of them who are not able to access the program overall.

Senator TOOMEY. Thank you.

Mr. Foster, do you have a comment on this?

Mr. FOSTER. Yes, I mean, I think that the main thing right now is for the type of business that you illustrated is to keep the business, because the business is in survival mode. And you need to let the business owner do what is necessary with the capital to keep the business alive. Certainly payroll is a part of it, but frequently they are behind on lease payments, and they could lose their facility. They have stretched their suppliers. You know, you just have to leave it up to the business owner because they really need—they are in survival mode.

Senator TOOMEY. Let me ask a question of Ms. Anderson. My understanding is that the Federal bank supervisors have made it clear that they will treat the Main Street Lending loans in a manner consistent with their supervisory approach to other commercial and industrial loans. So here is my question: If they were to change that and they were to take, say, a less restrictive view in their supervisory capacity, would bank behavior be likely to change? Or is bank behavior so driven by the existing set of internal rules that they would be unlikely to change?

Ms. ANDERSON. Thank you. So some bank behavior might change, but it may not be actually the behavior that is desirable overall. I think one thing to be clear is we do not think it is appropriate to have supervisory forbearance. The transmission of risk from the corporate sector to the banking sector is really not in the best interest of anyone, and certainly if you ask banks to go and make riskier loans right now, it might be okay for 12 months. But the credit problem will still be there just down the road.

So I think banks basically are looking at that, and even where supervisory requirements were relaxed somewhat, I think they can see that it is not worthwhile to rack up bad loans on their balance sheet that they will have to basically work out at some point in the future.

Mr. HILL. Thank you, Ms. Anderson. Senator Toomey, your time has expired.

Senator TOOMEY. Thank you.

Mr. HILL. The gentleman yields back.

We now have a second round of questioning for this panel, and I will yield myself 5 minutes to start that.

Some of these questions we are faced with today and that the Fed and the Treasury are faced with are not new questions. I would like to read a quote: "If it is a pawnshop in which necessitous borrowers are compelled to hock assets worth two to three times the amount of the loan, we are opposed, and we think most business people will be as well. We see no reason why the Government should be engaged in a careful pawnbrokering enterprise, niggling over security, haggling over interest, and competing with other lenders."

That was written back in 1933 as the Reconstruction Finance Corporation and the Fed struggled with how to get credit out to the American marketplace in a very tough economic recession of the 1930s, and I think we are dealing with that issue now in this middle-market segment that we are talking about today.

Mr. Foster, you offered some very good, constructive comments on specific loan term changes, but can you also address the affiliation question that I posed earlier?

Mr. FOSTER. Sure. Let me try to do that by giving you an example, and I want to compare and contrast with PPP. So when PPP, which used the same 7(a) program affiliation rules with relaxation for companies with an SBIC investment, the hospitality industry, et cetera, so you do not even have that in Main Street. So in PPP, if you had two commonly owned businesses that had 200 employees each, and they each had, you know, say $20 million in preexisting debt, they could each access up to $10 million of PPP for a total of 20. They needed to have the requisite cost structure that would do that.

You switch over to Main Street, two companies under common control, 7,000 employees each, each with $20 million in preexisting debt, 14,000 total employees, they have to share—if one of them wants to do the new loan facility, they have to share $15 million in total assistance under that program, and it really does not make any sense from an employee perspective, that 14,000 employees have access in total to a $15 million loan versus under PPP you had 400 employees that had access to up to $20 million.

So it really is poorly designed, and it does not make any sense for these kind of companies to have to run through really complicated and really severe 7(a) regulations that are really focused on making sure companies with more than 500 employees do not have access to a 7(a) loan.

Mr. HILL. Thank you. That is helpful. I appreciate that example.

Ms. Mills, let me turn to you and first echo the comments of our fellow Commissioners about condolences. So many of our families across the country have really suffered in this pandemic. We have to remember when we are doing our oversight work that, first and foremost, this is a public health crisis that has led to an extraordinary economic crisis. And so I appreciate the comments you made and the care you have for all of your members and your advocacy today.

And I also agree with Senator Toomey that the Main Street Program is not the solution to all challenges in this pandemic either, and that is why we have the unemployment compensation, the direct payments to our families, the forbearance in mortgage and rental payments, the payment for leave, the payment for testing, the flexible furlough program in the States so that people can be furloughed and maintain some benefits and get unemployment compensation, and obviously the aforementioned PPP. So all these Federal policies work together to try to minimize the impact on our families and help them get through the pandemic and also help get our economy back to full capacity.

In looking at your testimony, though, 74 percent of CMBS are less than $20 million, and in my district Asian American hotel owners are the classic small business entrepreneurs. And as I understand it, over 50 percent of hotel rooms are owned by these kinds of classic small business entrepreneurs across the country. And they are worried about getting October property tax payments in Arkansas, is, I know, one of their concerns, because they want to bring their staff back. They want to bring their staff back commensurate with the economy reopening. And, also, owners of CMBS securities are mostly pension funds and people's retirement accounts, and so they are all benefitted by trying to get capital into the industry and get people hired back and reopen.

So I am empathetic to your testimony. I thank you for being here very much and for your comments. But I think that the Main Street Program's mission is to try to get our hotel and hospitality open, and I hope we can find a such that does that.

Let me yield back and turn to my friend Mr. Ramamurti for 5 minutes.

Mr. RAMAMURTI. Thank you, Mr. Chairman.

Mr. Bohn, thank you for your testimony as well. I want to ask you the same type of questions that I asked Ms. Mills earlier. You come at this from a different perspective. You run a mid-sized company. Your organization represents a lot of such companies. But you seem to agree with Ms. Mills that this program has not been helpful so far. In fact, not a single one of your member companies has actually been helped by the Main Street Program so far. Is that right?

Mr. BOHN. That is correct.

Mr. RAMAMURTI. And it is in your testimony that the program needs to be changed. Can you describe the kinds of ideas you have in mind for that?

Mr. BOHN. Yeah, we list a couple of ideas in there that start with the removal of the affiliate exclusion, reducing the EBITDA requirements to make it more appealing to a broader class, particularly in the lower middle market, and we also talk specifically about the loan size and bringing the loan size down even further. Those are just some of them that we think—and, again, this is not only, you know, our team internally talking. These are is the direct comments we received back in the survey we just did.

Mr. RAMAMURTI. You also mentioned eliminating the restrictions on shareholder payouts and on executive compensation. Is that right?

Mr. BOHN. Correct.

Mr. RAMAMURTI. So, look, I agree with you on the diagnosis here, which is that the Main Street Program has not really helped anybody so far very much, and it is also unlikely to help a lot more companies without significant changes. But I am concerned about the proposed solution that you are offering. You propose changing the rules so that every company can get a loan even if before the crisis they had a lot more debt than they had earnings, you know, in other words, no matter how much risk there is that the public is going to end up holding the bag at the end of this. And at the same time, you propose eliminating restrictions on companies spending the loan money on payments to their shareholders and eliminating restrictions on executive pay. So I guess my question is: Why should the American people be willing to give billions of dollars to potentially failing companies that can just use that money to pay shareholders and executives while firing workers?

Mr. BOHN. Well, I think, Commissioner Ramamurti, when we talk about things like EBITDA and whether or not the company was at a higher risk prior, if you consider a large part of the lower middle market, which are oftentimes family-owned businesses, EBITDA in that case can be a misleading indicator because a lot of the costs and expenses roll through salaries and other types of things, and at the end of the day the EBITDA is not something significant. We see this a lot of times when purchases and acquisitions are made where there is a lot of debate and discussion over EBITDA and what is published through their regular financials.

So I think when we are looking at that, we tend to eliminate the opportunity for companies, particularly family-owned companies who are in that lower middle market, who at the end of the day their margins, their EBITDA are very, very limited and small, but yet they have been very successful for years, employ a number of different people.

Mr. RAMAMURTI. Can I ask just a follow-up question on that? On, let us say, the executive compensation restriction specifically, if a company exists that is not interested in the Main Street Program because of the executive compensation restriction, isn't it a fair guess to say that the reason that they are not interested is because they want to use some of that money to increase executive compensation? Otherwise, why is it a deterrent to them?

Mr. BOHN. Well, again, so that particular comment comes directly from some of our members of why they are not interested. What their particular reason for not being interested, I cannot go to that intent. But I will say that if there is anything that limits their ability to eventually sell the company upon paying the loan or to derive the benefits that they have built for building a company over time, I think that that is going to absolutely preclude them from wanting to utilize the funds that could otherwise be available to them.

Mr. RAMAMURTI. Thanks. Look, just to sum up quickly, I think we have actually seen a remarkable consensus emerge at this hearing, which is that the Main Street Program as currently designed is failing. The representative of the banking industry told us that we are not seeing meaningful demand for loans right now from their clients. The representative of small and mid-sized businesses told us that the program would not help its members as currently designed. And Ms. Mills, representing hundreds of thousands of workers, told us that the Main Street Program has not helped a single worker and is not likely to.

I do not question the hard work of President Rosengren and the Fed staff, but more loans are not going to solve this crisis. Struggling small and mid-sized companies cannot take on more debt right now, so the only tool in the Fed's belt is the wrong one. This program was given $75 billion and months to succeed. It did not and it cannot. It is time to stop tinkering around the edges with adjustments to loan eligibility and loan terms when the fundamental problem is with the nature of the loans themselves.

It is time for Congress to step back in so that we can actually save small and mid-sized businesses, and when it does, it needs to tie the assistance to meaningful, enforceable protections for workers, and not just hand money to executives and trust them to take care of workers' interests.

Thank you, Mr. Chairman.

Mr. HILL. The gentleman yields back, and we now turn to Congresswoman Shalala for 5 minutes.

Ms. SHALALA. Thank you very much.

Ms. Mills, one of the problems with the loan program, it seems to me, including this program, which clearly has flaws in it, is that loans protect the health care of executives but not of workers. Nothing that we have done—unemployment insurance to support workers—protects their health care, unless these hotels, for example, furlough people and keep their health care.

So, fundamentally, what the Fed has done will protect the health care of a lot of executives, but there is nothing that we have done, particularly in the unemployment insurance system, that protects the workers' health care. I think that was one of your points.

Ms. MILLS. Yes, thank you. That is correct that the extension of the wages that the Congressman mentioned has been appreciated, although it is now ending. That is problematic. But there has not been an extension of health care. And even in a case where we have some health care negotiated, companies like the Fontainebleau, you know, are not abiding by that. So that is absolutely correct.

Ms. SHALALA. Thank you.

Ms. Anderson, three of the five facilities require that Main Street loans be senior or pari passu with, in terms of priority and security, the borrower's other loans or debt instruments other than mortgage debt. Are lenders willing to subordinate or dilute their priority and security? What impact does this provision have on an applicant's ability to borrow under the Main Street Lending Program?

Ms. ANDERSON. Thank you for your question. This is a true issue in the sense that many mid-sized companies have existing debt structures and having senior credit come in at this point basically has to be negotiated with those existing lenders, many of whom are not bank lenders, and that then becomes a complex process in terms of an inter-creditor agreement. And I know that has certainly put off some borrowers in terms of trying to go through that process when you may not receive the consent from the other lenders who may just not have the same incentives as the originating bank. So it is a problem, and it is complex.

Ms. SHALALA. Thank you.

I have a question for Mr. Bohn. In your written testimony, you stated that the challenges with the Main Street Lending Program have a lot to do with whether people actually understand it. Do you have some specific recommendations in that regard?

Mr. BOHN. Thank you, Congresswoman Shalala, and as I am sitting here in Orlando, Florida, thank you for representing our great State here on the Commission and in general.

So, yes, I think that one of the things we heard back from our survey was that there was—unlike the PPP, where there was significant awareness about the various provisions and tenets of it, there was a lot more ambiguity and misunderstanding. Some of that related to how long it is taking for the program to come together, some of that because there was a little bit of misunderstanding thinking that it would be different than PPP because it was loans and not carve-out 501(c)(6)'s or affiliated groups.

So I think that there is an opportunity here, regardless of where the changes are made, to make sure that the program is much more clearly communicated on a wider basis, and we are willing and able to help with that in any way we can.

Ms. SHALALA. Do you have a specific recommendation on the loan size?

Mr. BOHN. Well, I have a specific recommendation on the loan size that it should come down to closer to $50,000, and here is what makes me say that. There were a number of smaller family-owned businesses in the middle market that I have spoken to recently right here in Orlando who have said, look, we do not need $250,000 but we do need $50,000 or $75,000 in order to prepare what we think is going to be a longer haul to deal with the fallout from COVID, whether that is safety equipment or how we run our operation. But $250,000 is too large of a haul for them, and, again, do not want to get out over their skis financially. So, yes, a specific recommendation on that, yes, ma'am.

Ms. SHALALA. Thank you. I yield back.

Mr. HILL. Thank you, Congresswoman, and now we will yield to Senator Toomey for 5 minutes.

Senator TOOMEY. Thank you very much, Mr. Chairman. This has been very, very helpful and informative, and I really appreciate the testimony of all of the participants.

My own view is it is way premature to come to the conclusion that this has all been a failure. Okay, I think there are definitely some improvements we ought to be looking at, and there might be entire new versions of Main Street Programs that we ought to contemplate. We talked about affiliation rules, which I think need to be changed. There may be terms that ought to be modified. I am interested in something that would be more asset-based rather than just income-based.

But let us keep in mind it took a long time to get this up and running. That was always going to be the case because of the nature of the complexity of doing this kind of funding. There has been a recent acceleration in use. If the acceleration continues, we may see significant pickup.

Mr. Bohn makes the argument that there is a high level of unawareness or low level of awareness about this. There is a lot we could do to remedy that which could result in more participation.

And then, finally, this leads to my question. You know, I would argue that the corporate bond programs, which are not the ones we are here to talk about today, but the 13(3) facilities that set up the corporate bond-buying programs have been enormously successful despite the fact that the Fed has purchased very, very few bonds. It was the standing up of the program, the existence of the program, that allowed the private market to operate, to operate actually at an all-time record volume, after having been frozen. That is a remarkable success story, despite the fact that there was not a lot of history.

So that gets me to my question, and maybe I should have asked this at the beginning, and, Ms. Anderson or Mr. Bohn or Mr. Foster, any of you might have a thought on this. But how should we best determine objectively the extent to which credit needs are being met or not being met? I have heard anecdotally from Pennsylvania companies and Pennsylvania banks that when this pandemic resulted in a shutdown, there was a massive drawdown on existing credit lines. People piled up as much liquidity as they possibly could. Then after a little time passed, they started to pay down some of those balances. But, you know, we can certainly seek bankruptcy filings; at that point it is kind of too late.

What should we be looking at on a day-to-day basis, what metric should we be using to determine how significant the unmet credit demands are in this space? And, Ms. Anderson, maybe you could lead it off.

Ms. ANDERSON. Sure. Thank you. So I think you make a good point in that, by and large, credit demands for many companies are being met. We saw record lending from banks early on in the pandemic, so $700 billion plus was lent over the course of 3 months.

Since then, we have seen about $200 billion in that C&I lending space be repaid, so I think you are right, businesses are, you know, paying down some of that liquidity that they took in in the early days of the crisis.

And speaking to our banks, the demand for credit has lessened. They are not getting millions of inquiries from their customers, new or existing. And I think that really says something, and they have all been segmenting their books trying to see who needs credit or other solutions, and I think really is a temporary liquidity credit need, then the banks by and large are providing that. If it is a solvency need, that is not something that banks provide to companies.

Mr. FOSTER. Senator, I think one simple way to figure out if there is unmet credit needs is to ask the banks how many Main Street loans have been requested by borrowers that the banks have rejected. If you could capture that data, you would get a real good idea, because I am aware of probably a hundred. And it is not the banks' fault. You know, we have a restaurant group in Florida and the bank who signed up for the program said, "I cannot take any more restaurant exposure in my portfolio," because they are approaching it like a bank. They are not approaching it differently. They are not relaxing underwriting standards. If you are a restaurant group, you are not getting a bank loan. And if we do not capture that data, you figure it out.

Senator TOOMEY. I think that is a very interesting point.

Ms. Anderson, is there a way that that data is being collected systematically so that we could access that? Or does that not exist in a centralized place?

Ms. ANDERSON. So it is not being collected systematically at this point in time. Certainly we could work with our members to get you additional data on that in terms of our members who are active in the program. They are receiving between 500 to maybe 2,000 inquiries in relation to the Main Street Loan Program, and as I said before, you know, upwards of three-quarters of those actually do not understand the program and think it is a grant program. So it is really not a high level of inquiries even.

Senator TOOMEY. Thanks very much. Mr. Chairman, I see my time has expired.

Mr. HILL. I want to thank our witnesses again, both panels. Excellent discussion. I want to thank our Commissioners for their participation today and for their thoughtful questions. And on behalf of the Commission, in addition to thanking the witnesses, let us thank the staff as well for their preparation in putting the hearing together.

This hearing is adjourned.

[Whereupon, at 12:04 p.m., the Commission was adjourned.]

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